Winning in Asia

Creating long-term value

A SPECIAL REPORT

Asialink Business | Australian Institute of Company Directors | Chartered Accountants™ Australia + New Zealand | CommonwealthBank

Supported by BCG Boston Consulting Group

The Sid and Fiona Myer Family Foundation

On behalf of all project partners, Asialink Business extends sincere appreciation to The Sid and Fiona Myer Family Foundation for its generous and founding support of this project. In particular, we thank Sid Myer for providing the vision for this project and for his constant encouragement and support.

Thank you to our knowledge partners

BCG BOSTON CONSULTING GROUP

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CONTENTS

JOINT PARTNER INTRODUCTION 04

WINNING IN ASIA IN THE MIDST OF COVID-19 AND BEYOND 07

EXECUTIVE SUMMARY 14

DOES OFFSHORE EXPANSION LEAD TO SUPERIOR RETURNS? 17

HOW THE BEST 'WIN IN ASIA': BUSINESS MODELS FROM COMPANIES SUCCEEDING IN ASIAN MARKETS 27

MATCH FIT 2.0: CREATING ASIA-CAPABLE LEADERS 69

BEST PRACTICE IN EXTERNAL AFFAIRS: MANAGING YOUR STAKEHOLDERS, BRAND AND REPUTATION IN ASIA 87

A STRATEGIC APPROACH TO WINNING IN ASIA 97

NOTES 103

GLOSSARY 105

ACKNOWLEDGEMENTS 106

JOINT PARTNER INTRODUCTION

'The rise of Asia' or 'the re-emergence of Asia' does not reflect the reality of Asia's place in the world today. Sustained economic performance and geostrategic forces have ensured that world economic weight is firmly centred in our region.

Successive Australian governments over the last 50 years have fostered deep economic relationships with the countries in our region. The range of free trade agreements concluded in the last five years alone is reflective of the continued progress made. With seven of our top 10 trading partners in Asia, and a growing proportion of cross-border investment with Asia, our economy is inextricably linked to the region. Migration flows, international students and tourists from the region, and our increasingly multicultural workforce confirm our deep connections with the region.

The impact of the novel coronavirus, a black swan event, has not been discriminatory. The devastating impact of the virus on the health, wellbeing and prosperity of nations across the world has been profound. Australia has to date managed its response to the pandemic highly effectively. Australia is one of the few countries to have had its economic forecasts revised by the IMF at mid-year to reflect improving economic prospects.

There is no room for complacency. The impact of the virus in waves on many of the countries in our region has highlighted that any prolonged recovery for Australia will be highly dependent on our partners in the region.

Winning in Asia has never been more important to Australia's economic prosperity and security. Going forward, sustainable long-term growth in the performance and returns of Australian businesses will be even more dependent on Asian markets. Winning in Asia's highly competitive markets will be central to sustaining our per capita income levels, adding sustainable jobs to the workforce, and growing our long-term pool of national savings. Our largest companies will be central to this proposition.

Two years in the making, *Winning in Asia: Creating long-term value* is a project that seeks to dispel many of the commonly held perceptions of the challenges of doing business with the region. It seeks to provide fresh, evidence-based analysis which makes a compelling case for why our largest companies should increase their exposure to Asian markets. This report, which details the findings and recommendations from this project, considers major questions posed over a long period of time by Australian business leaders, policymakers and investors.

For instance, does offshore expansion lead to superior returns for the shareholders of Australian companies? Which companies – Australian and non-Australian – have grown market share, profitability and returns in Asian markets? What are the capabilities Australian boards and senior executive teams need to enable their respective organisations to succeed in Asian markets? And, how can Australian companies best manage the risks associated with doing business in the region?

Together with a taskforce of some of Australia's pre-eminent business leaders and our knowledge partners, we have considered these questions, which have profound implications for the Australian business and investor community and government.

With over 300,000 data points of evidence-based analysis, the findings and recommendations require critical consideration to ensure a long-term sustainable recovery from the pandemic.

We are proud to have brought together the insights, capabilities and connections of Asialink Business, the Australian Institute of Company Directors, Chartered Accountants Australia and New Zealand, the Commonwealth Bank of Australia, and The Sid and Fiona Myer Family Foundation.

This report is a call to action to Australian businesses to understand the factors essential to win in competitive Asian markets. We hope it replaces uncertainty with confidence, myths with reality, and a local mindset with a global mindset with Asia at its core. Australia's future prosperity depends on it.

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Winning in Asia in the midst of COVID-19 and beyond

WINNING IN ASIA IN THE MIDST OF COVID-19 AND BEYOND

THE IMPACT OF THE PANDEMIC ON GLOBAL GROWTH

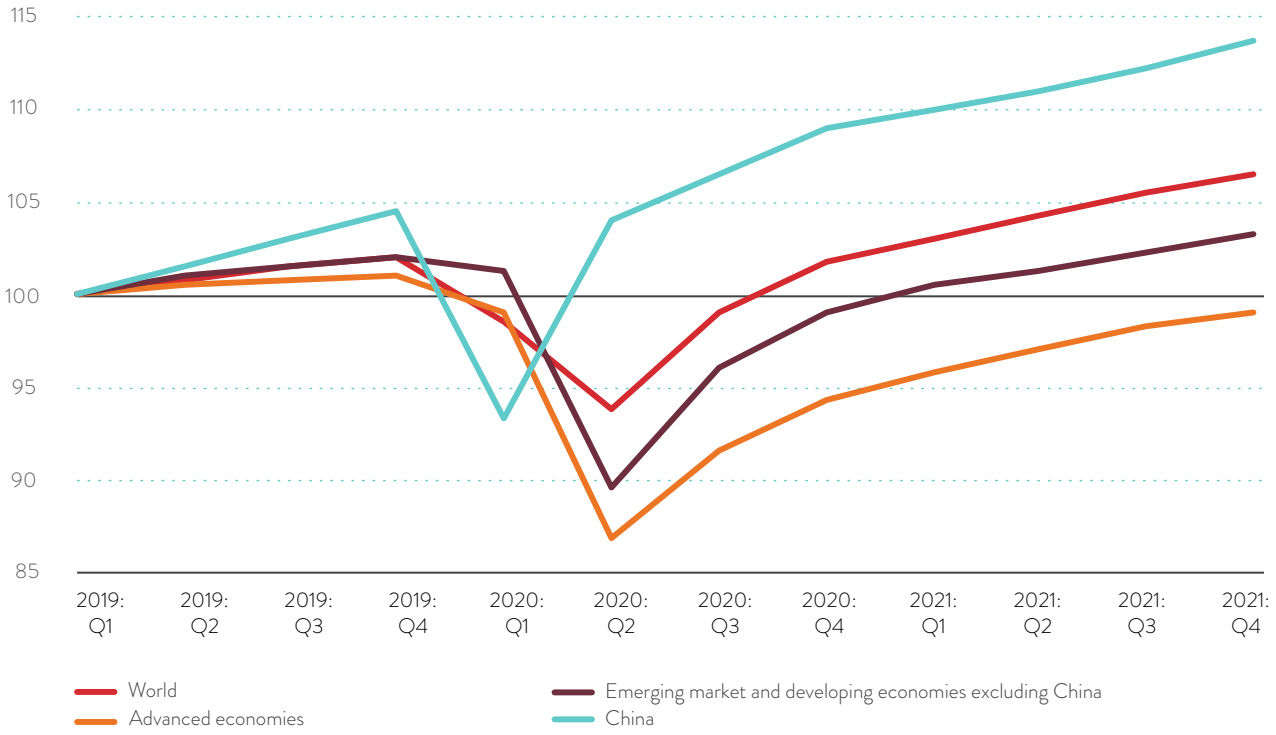
Global growth has been dramatically impacted by the COVID-19 crisis, projected at an alarming -4.9 per cent in 2020, the worst economic downturn since the Great Depression[1]. The multiple waves of the pandemic, the synchronised deep global downturn, depressed consumer spending, mobility restrictions, and contraction in global trade have had an unprecedented impact on the global economy[2].

The IMF forecasts that all major advanced economies are projected to record growth worse than -4.9 per cent. China, India and the ASEAN 5[3] are all projected to record growth rates better than the major advanced economies and the global growth rate. China is forecast to grow at 1 per cent, India at -4.5 per cent, and the ASEAN 5 at -2 per cent[4]. Australia is now forecast to record -4.5 per cent growth in 2020, two percentage points better than the April forecast[5]. The successful containment to date of the virus and gradual easing of restrictions on business are amongst the reasons cited for the improvement in Australia. The Australian Government's own forecasts (as part of its Economic and Fiscal Update in July 2020) reveal that the economy is forecast to record -2.5 per cent growth in the current financial year and that unemployment is expected to be -8.75 per cent in the same period. On a calendar year basis, the contraction is expected to be -3.75 per cent in 2020[6].

The OECD is less positive on the state of the Australian economy, noting a likely contraction of -5 per cent in 2020[7].

FIGURE 1. ***Quarterly world GDP***

(2019:Q1=100)



Source: IMF staff estimates.

The impact of the pandemic challenges the broadly heralded pre-pandemic view of the Asian Century. Consistently cited projections over the last decade have held that the real GDP of Asian economies are projected to exceed the combined economies of the Americas and Europe by 2030[8]. Asia is also expected to account for over 70 per cent of world capital stock by 2030 and lead capital exports[9]. Even sooner, by as early as 2020, the middle class consumers in Asia were expected to outnumber the middle class consumers in the rest of the world combined[10]. These macro-level narratives have influenced national, industry and firm-level agendas in Australia and across the world in respect to the scale of opportunity in Asian markets.

As Prime Minister Lee from Singapore recently highlighted, notwithstanding the extraordinary economic growth in Asia "an Asian Century is neither inevitable nor foreordained"[11]. While this assessment is a sobering reminder of the impact of geostrategic tensions between China and the US, regional tensions and the impact of the pandemic, it should also be viewed in a relative context. From an economic perspective, projections of the region remain that it will continue to be the growth engine for the global economy and the macro-level narratives of the size of the opportunity in Asia still retain their value[12]. Realising the opportunity however, may be more complicated, requiring greater government-to-government engagement, deeper business-to-government engagement, and a recognition that economic, defence and strategic national interests will prove increasingly harder to decouple.

Navigating the new normal: Shocks, tensions and contradictions

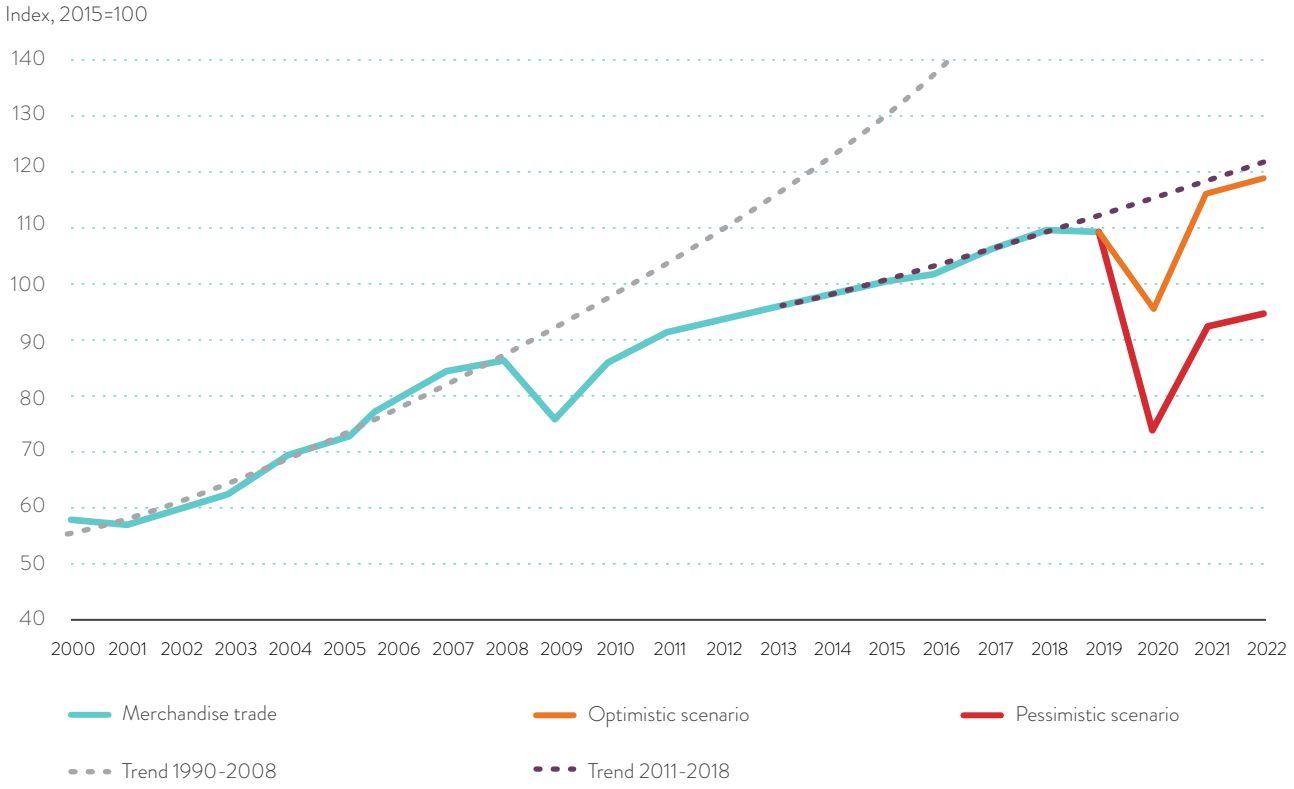
Globalisation has come under sustained attack in 2020. Reshoring to enable supply chain resilience and drive sovereign capability has become a popular rhetoric of governments internationally. Martin Wolf (in referencing Sebastien Miroudot from the OECD) reminds us of the difference between 'resilience' and 'robustness':

> The former refers to the ability to return to normal operations after a disruption; the latter to the ability to maintain operations during a crisis. In a pandemic, the latter is probably the more relevant. The obvious way to achieve robustness is to diversify suppliers across multiple locations[13].

While a singular focus on sovereign capability may impede the realisation of economies of scale, the cost of maintaining multiple supply chains, while seemingly robust, could actually become a very costly exercise.

Alarmingly, the impact of the pandemic has gone beyond a desire to ensure resilience. It has seen a precipitous fall in trade and investment. Steven Altman cites the WTO, UNCTAD and ICAO to highlight globally "a 13-32 per cent decline in merchandise trade, a 30-40 per cent reduction in foreign direct investment, and a 44-80 per cent drop in international airline passengers in 2020"[14].

FIGURE 2. ***World merchandise trade volume***



Source: WTO/UNCTaD and WTO Secretariat estimates.

There have been significant impacts felt by Australia, most notably on the international education and tourism sectors. Universities Australia forecasts a $16 billion hit to Australian universities due to COVID-19 by 2023, with revenue losses in 2020 now forecast to be between $3.1 billion and $4.8 billion[15]. The tourism sector is forecast to take a hit of $55 billion in 2020 relative to the $138 billion of expenditure in the sector in 2019[16].

On the other hand, the iron ore sector has had strong demand, prices and uninterrupted supply chains. The agricultural sector has reported minimal impact from COVID-19[17]. The Australian Government has played an important role in neutralising the impact of COVID-19 on the sector through targeted support in air, freight and logistics services. Across 11 commodity categories, the Australian Government has attributed the impact of COVID-19 on only two categories, seafood, meat and live animals. The impact on these two sectors is not immaterial. For instance, there is an expected fall of $200 million in seafood export earnings with China in 2019-2020 attributable to the pandemic[18].

There has also been exponential growth in e-commerce, with Australia Post reporting an 80 per cent increase in year-on-year sales in the eight weeks after the COVID-19 pandemic was declared by the World Health Organization[19].

Australia's position appears steadfastly in support of globalisation. The Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA), which came into effect on 5 July, marks yet another free trade agreement by the Australian Government to create preferential market access with a key economic partner. Ongoing significant efforts to engage more deeply with India, in addition to the India Economic Strategy to 2035 (IES), including through the recent virtual summit between prime ministers Morrison and Modi in June 2020, is reflective of the efforts being made to enable trade diversification strategies in both markets.

Australia remains heavily coupled with Asia from a trade and investment perspective. Seven of our top 10 trading partners are in Asia, and an increasing volume and deal value of inbound investments have come from Asia over the last decade, most notably from China, which still remains behind Japan in its stock of foreign direct investment in Australia[20]. The US remains by far the largest investor in Australia.

Australia has also grown its outbound investments in Asia. Over the last 10 years Australian investment in Asia has grown almost four-fold from $120 billion in 2009 to $472 billion in 2019[21]. While it is true that Australia still invests more in New Zealand than it does in China and almost six times more than it invests in India (based on 2019 investment levels), the levels of Australian investment in Asia are steadily rising.

Key drivers of Australian engagement with Asia

Our analysis suggests that there will be five key drivers underpinning Australian engagement with Asia in a COVID-19 and post COVID-19 environment.

1. International cooperation will be 'more, not less, important'

We believe that rather than a retreat to protectionist measures, Australia will continue to recognise that its future is inextricably linked to Asia. As our consultations have highlighted, in the sensitive area of healthcare, international cooperation will only become more important. For instance, with their large populations, Asian countries will serve as critical for Australian clinical trials in cardiovascular diseases or diabetes. In the midst of COVID-19, with significant rhetoric favouring sovereign capability, Australian researchers have been working with partners from the US, Asia and Europe to find a vaccine for the virus. The need for cooperation on grand challenges will continue to be self-evident.

2. Digital trade

The exponential growth in e-commerce highlighted previously and replicated across the world is highly likely to continue into the future. As McKinsey & Company highlights, consumers are accelerating adoption of digital sales channels and most first-time users are either satisfied or very satisfied with their experience and the majority plan to continue using digital channels in a post COVID-19 environment[22].

As recent business performance highlights, Australian health and wellness companies have seen an increase in activity levels in China[23]. We expect long-term e-commerce opportunities across China, South-East Asia and India for Australian companies.

3. International diversification for long-term value (China "plus")

Australia remains one of the few countries in the world with a trade surplus with China. Sectors of the Australian economy, such as the mining sector, have deep long-term relationships with Chinese customers. The size of the Chinese market for Australian miners indicates that there may not be an equivalent alternative market. This suggests a 'China plus' strategy[24].

Customer diversification is generally well-understood by companies as they have to actively manage the risks of overexposure to one or a few customers. Developing alternative markets and customers is an increasing priority for Australian companies. The size of the domestic market will continue to drive Australian companies – large and small – offshore for growth. This offshore expansion will also increasingly couple trade with outbound investment, that is, investment will be necessary to be close to the end consumer. This will be particularly the case with the services sector.

4. Internationalisation is first about international best practice

The continued rise of Asian multinationals, technology companies and universities is likely to drive technological trends, management practices and leadership approaches going forward. Learning from Asia rather than teaching Asians best practice will increasingly become the norm. With several Chinese, Indian, Japanese and South Korean companies being global leaders across verticals, they are highly likely to be natural partners for Australian companies in third country markets in the region. Strategic alliances and joint ventures with Asian companies could involve significant technology and knowhow spillovers to Australian companies.

5. Regionalism is the new globalism

As McKinsey & Company highlight, a growing level of Asia's trade is intra-regional as is its cross-border investment[25]. For instance, 60 per cent of goods traded are within the region, 59 per cent of investment is intra-regional and 74 per cent of Asian travellers travel within the region. This means that Australia will need to increasingly compete for a share of Asian trade, investment and tourists as they increasingly migrate towards integration within their own region.

OUR APPROACH AND METHODOLOGY TO WINNING IN ASIA

The focus of this report is on addressing the various misconceptions Australian boards, senior executives and investors have of the challenges of doing business with the Asian region. We address the perceived challenges with rigorous, evidence-based analysis across four areas:

1. The relationship between offshore expansion and returns

We examine the relationship between market diversification and returns to understand if internationally diversified companies perform better than those that are domestically focused. This is a threshold question essential to influence Australian business leaders of the size, scale and quality of the market opportunities in Asian markets. We compare the ASX 200 to peer companies from other regions, evaluate the total shareholder returns of internationally diversified and domestically focused companies, and assess the factors that support internationalisation.

2. Business models to succeed in Asia

We apply a three-part framework to understand business models, including, criteria for assessing opportunities in Asia, capabilities to execute and modes of entry. We examine case studies of non-Australian and Australian companies that have successfully entered Asian markets. We use a combination of quantitative evidence of market share, performance and returns (with the non-Australian company case studies) and qualitative commentary developed with C-suite executives (with the Australian company case studies) to draw out the specific strategies and business models that have led to success. We cover a mix of public and private companies.

3. Capabilities to execute in Asian markets

We assess the Asia capabilities of the boards and senior executive teams of the ASX 200 to understand if our senior leaders have the capabilities to create and execute strategies in Asian markets. Using a proprietary methodology, we study over 100,000 data points of evidence of Asia capabilities in a pool of 1,705 board members and senior executives. Through extensive stakeholder consultations of senior leaders we identify constraints on our companies engaging effectively with Asian markets and make specific recommendations to overcome the constraints.

4. External engagement for risk mitigation and impact

We assess the critical impact of external affairs to manage stakeholders, brand and reputation in Asian markets. We compare and contrast Australian external affairs functions to their international counterparts, evaluate the optimum size, composition and focus of external affair teams, and present new ideas to foster more effective media and communications engagement by Australian company executives.

Key principles driving our approach:

1. **Co-development:** The report reflects the collaborative partnerships developed with knowledge partners including the Boston Consulting Group, Cooper Investors and Ellerston Capital. These partners were seen as critical to complementing Asialink Business' strengths in providing rigorous, evidence-based quantitative analysis for the first two sections of the report (on international expansion and returns and business models). Asialink Business ensured a similar rigorous approach to the third and fourth focus areas of the report (on capabilities and external affairs respectively).

2. **Stakeholder consultations:** Co-development with knowledge partners was complemented with extensive stakeholder consultations with senior leaders, typically board members and C-suite executives of Australian public and private companies. The consultations ensured that there was incisive qualitative commentary to support the quantitative findings.

3. **Focused data set:** The data set focuses primarily on the ASX 200. The ASX 200 was a focus of the report as a result of significant stakeholder consultations over the last five years indicating that there was a perception that this segment of the Australian workforce was underweight with its engagement with Asian markets. The ingenuity of small and medium enterprises (SMEs) has been recognised in other significant research. For instance, recent research undertaken by Asialink Business with the Commonwealth Bank of Australia has focused heavily on SME engagement with Asia[26]. In *Winning in Asia*, we selectively complement the analysis on the ASX 200 with analysis of private companies to compare and contrast their orientation, business models, leadership capabilities and mindset.

4. **Data-driven:** Our analysis in this report includes over 300,000 fresh data points of analysis. An important principle for the project partners was to ensure that the direction, findings and recommendations presented in the report reflect genuinely new, well-researched, and evidence-based analysis.

5. **Strategies based on evidence:** The final section of the report presents strategies for our corporate sector, government, peak bodies, and the broader workforce to drive a winning formula with Asian markets. Each strategy prescribed is based on evidence-based findings reflected in the report.

Diversification – Markets, services and models

Previous Asialink Business research has highlighted that accessing non-resource sector opportunities in Asia with the right business models and capabilities could add up to $275 billion to the Australian economy[27]. Asialink Business' research has also highlighted that driving greater services sector engagement with Asia could add more than one million jobs to the Australian economy by 2030[28]. Combining the strengths of our resources sector with the potential of our services sector provides us with an exceptional portfolio of companies that can pursue opportunities with Asia.

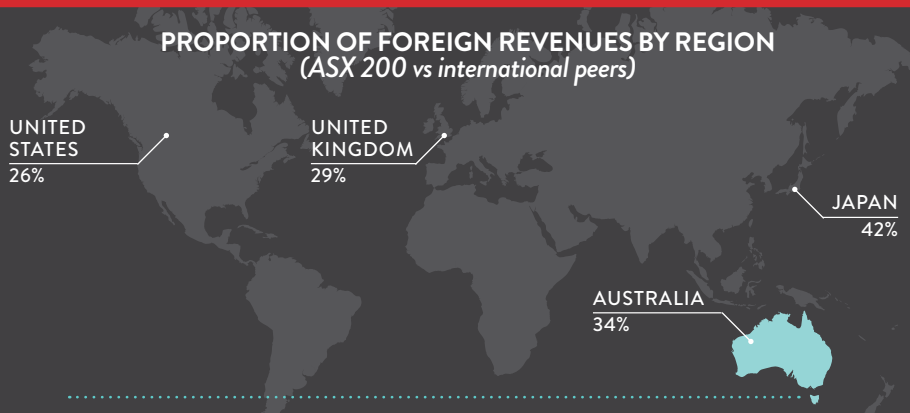
Our top companies are central to realising these goals. This report focuses on ensuring that they access the right opportunities, execute the right business models, utilise the best capabilities and navigate risks effectively. In the current low to negative growth environment with high levels of unemployment, winning in Asia through the blueprint in this report is essential.

Executive Summary

WINNING IN ASIA: CREATING LONG-TERM VALUE

1. AUSTRALIAN COMPANIES ARE BECOMING MORE INTERNATIONAL

PROPORTION OF FOREIGN REVENUES BY REGION
(ASX 200 vs international peers)



Internationally focused ASX 200 companies create more value than domestically focused companies

82% MORE TSR (MARKET CAP $2BN-5BN)

36% MORE TSR (MARKET CAP >$5BN)

Amongst the ASX 200, multiple sectors are predominantly international
% of offshore revenues

>70%
- Materials
- Healthcare
- Information Technology

>25%<50%
- Div. financials
- Real estate

<25%
- Industrials
- Comm. services
- Energy
- Consumer discretionary
- Banks
- Consumer staples
- Insurance
- Utilities

ASX 200 Asia Pacific (APAC) revenues have grown the most between 2014 and 2019

↑ 8.5% p.a.

EMEA, Americas and other market share of total foreign revenues

58% | **42%**

APAC share of total foreign revenues

2. BUSINESS MODELS TO DELIVER SUPERIOR RETURNS DEPEND ON THREE THINGS

Clear evaluation criteria

Size of the prize | Potential for play | Right to win | Path to achieve

11 Asia capabilities

Individual | Organisational

Executing through the right business mode

Agent/distributor, E-commerce, Licensing, Strategic alliances, Corporate venture capital, Wholly owned subsidiary, Joint venture (JV), Mergers and acquisitions (M&A), Listing in host country

Case studies to show how business models drive market share, profitability and returns

3. MATCH FIT ASIA-CAPABLE SENIOR LEADERS ARE ESSENTIAL TO ENABLE SUCCESSFUL ASIA EXPANSION STRATEGIES

OVER 90% ARE NOT ASIA-CAPABLE (>50% ASIA CAPABILITY SCORE)

13.8% Average Asia capability of board members

13.5% Average Asia capability of senior executives

80%
of companies that have above average Asia capability generate over 40% of their revenues from Asian markets

4. STRENGTHEN EXTERNAL AFFAIRS TO MANAGE STAKEHOLDERS, BRAND AND REPUTATION IN ASIA

>50% of market value is attributable to reputation in key Asian markets

[Weber Shandwick, 'The State of Corporate Reputation in 2020: Everything Matters Now']

The external affairs function of Australian companies in Asia is often smaller than European and US companies

Media sentiment in reporting on Asia related business and economic issues is not strongly positive, negative or neutral relative to business reporting on the US or Europe

EXECUTIVE SUMMARY

DOES OFFSHORE EXPANSION LEAD TO SUPERIOR RETURNS?

1. **Australia's largest listed companies are becoming more internationally diversified,** as measured by the proportion of revenues generated in foreign markets. **ASX 200 companies generate 34 per cent of their revenues from foreign sources,** more than the largest listed companies in the UK (29 per cent) and US (26 per cent), but less than Japan (42 per cent). This is largely driven by the mining and materials sector. In consumer discretionary, consumer staples, energy and industrials ASX 200 companies generate the lowest proportion of offshore revenues compared to peers from these other regions.
2. **The share of revenues from foreign sources among ASX 200 companies has increasingly been driven by exports to the Asia-Pacific,** which accounts for 42 per cent of the share. From 2014 to 2019, the number of companies exporting increased by around 10 per cent, while five additional companies generated over 70 per cent of their revenues offshore.
3. **In Australia, industry dynamics have significant influence on the decision to expand overseas.** High domestic market saturation, opportunities to achieve economies of scale in sales volumes to offshore markets, and a high level of cross-border flexibility and low levels of regulation are some of the factors that influence offshore expansion. In 2019, the materials, healthcare and information technology sectors all generated 70 per cent or greater of their revenues offshore. Subject to ongoing industry dynamics, significant upside remains in offshore expansion in consumer discretionary, consumer staples, banking and the insurance sectors, all of which currently generate less than 10 per cent of revenues offshore.
4. **There is evidence to suggest that, among larger companies, those that are internationally diversified create more value for shareholders** than companies that are domestically focused. For the medium ($2b-5bn) and large ($5bn+) market cap groups, the internationally diversified group outperformed the domestically focused group on average in long-term value creation, measured by a five-year Total Shareholder Return (TSR) from 2014 to 2019. Internationally diversified companies in the medium group achieved on average 82 per cent more shareholder returns, while in the large group they achieved on average 36 per cent more shareholder returns. This outperformance by large, internationally diversified companies generally holds within industries as well.
5. **There is no uniform answer to offshore expansion.** It requires sound strategic rationale supported by strong execution. There is no 'one size fits all' answer to international expansion; business leaders should assess geographic expansion against other growth opportunities on a case-by-case basis. This observation is supported by analysis of the complete ASX 200 dataset which finds no uniform relationship between a company's geographic revenue mix and its TSR.

HOW THE BEST 'WIN IN ASIA': BUSINESS MODELS FROM COMPANIES SUCCEEDING IN ASIAN MARKETS

1. **Our research emphasises a three-part framework to considering and applying business models in Asia.** This includes a model to clarify criteria to pursue opportunities, a capabilities framework to execute and modes of entry. We profile 22 case studies of companies succeeding across markets and sectors.

2. We focus our research on the **success of local and non-Australian multinationals in China** over the last two decades. Key factors include the 'consumption upgrade' by Chinese consumers, the rise and influence of the internet, cultural change in Chinese business practices (impacting product development, business processes, and marketing), the integration of international brands, marketing and distribution across Tier 1, 2 and 3 cities, and the critical use of customer data to drive decision-making. **We use case studies in infant formula, sportswear, food service, hotels, and technology to illustrate how customers, revenues and operating profits can be grown in China.**
3. Our research on the **success of multinationals in India highlights a breadth of criteria, capabilities and entry modes adopted to succeed.** Case studies across the automotive sector, FMCG, diversified financials, and insurance illustrate a breadth of business models that have led to significant market share, returns and profitability. **Through our analysis of returns generated, we highlight how the Indian operations have become the most valuable asset of various multinationals.**
4. We showcase **a new selection of Australian companies** that have succeeded in Asian markets. The sectors covered include consumer staples, consumer discretionary, property, construction and infrastructure, technology, healthcare and financial services. A range of entry modes from joint ventures and wholly owned subsidiaries to acquisitions are presented to highlight that Australian companies – led by Asia-capable leaders – across sectors, bring world-class strategic thinking, products and services, technology, and relationships to succeeding in Asia.
5. **We contrast Australian public companies with private companies** and identify that private companies distinguish themselves across three key criteria in their approach to engaging with Asian markets: relationships with family-owned companies in Asia, long-term orientation, and the use of patient capital.

MATCH FIT 2.0: CREATING ASIA-CAPABLE LEADERS

1. **The average Asia capability scores for board members and senior executives in the ASX 200 are 13.8 per cent and 13.5 per cent respectively.** Importantly, only seven per cent of board members and senior executives would qualify as Asia-capable (that is, have a score greater than 50 per cent). **This means that over 90 per cent of senior leaders (board members and senior executives) in the ASX 200 would not qualify as Asia-capable.** These results are concerning as our research has consistently found that companies with an above average level of Asia capability in their senior leadership generate a greater proportion of their revenues from Asia.
2. **We found that leaders were, on average, strongest in their knowledge of Asian markets and weakest in their ability to adapt to Asian cultural contexts.** This suggests that while Australian business recognises the need to understand the market opportunity presented by Asia, this knowledge is not yet matched by an appreciation of the cultural skills needed to execute on those opportunities.
3. We found that financials, consumer staples and materials were the sectors with the highest number of Asia-capable board members and consumer discretionary, materials, financials and consumer staples had the highest number of Asia-capable senior executives.
4. What these results indicate is that, subject to industry dynamics, there is significant upside potential in our consumer staples and consumer discretionary companies assessing and executing opportunities with Asian markets. They are underweight with their international exposure while they have amongst the highest number of Asia-capable senior leaders. Our materials and diversified financial companies are already strong with their international exposure.

   Our banks and insurance companies are very low with their international exposure but they have had significant experience already in evaluating opportunities with Asian markets across a range of products and services. The value of Asia-capable senior leaders to our banking and insurance sectors may lie in their understanding of international best practice in governance, risk management, technology and management.

   Finally, the results indicate that for as long as we remain export-driven in commoditised sectors, the relative need for Asia capabilities in board and senior executive teams may be lower. **As we transition to more outbound investment, typically in more services driven sectors, the relative value of Asia capabilities will increase.** Consequently, as we seek to export a greater proportion of services to the Asian region, Asia-capable senior leadership will be critical to successful offshore expansion.

EXTERNAL AFFAIRS: MANAGING STAKEHOLDERS, BRAND AND REPUTATION IN ASIA

1. **A strong, well-resourced external affairs capability is important for navigating business opportunities in Asia, especially for investors.**
2. Most Australian companies operating in Asia have a limited external relations presence in the region, including at the individual country level. Of the larger Australian companies, some have external affairs representation in regional headquarters. However, the size of the external relations presence is often smaller than US or European company teams. **Building adequate strength and quality in external affairs teams is essential to managing critical risks related to matters such as bribery and corruption**, influencing policy and actively managing the corporate brand and reputation.
3. Our research highlights that, over the last three years of media reporting on economic and business issues, **there is limited evidence to suggest that the media is more or less positive, negative or neutral on Asia** than other regions, in particular the US.

Does offshore expansion lead to superior returns?

DOES OFFSHORE EXPANSION LEAD TO SUPERIOR RETURNS?

By Damien Wodak, Managing Director and Partner, and Daniel Selikowitz, Partner, Boston Consulting Group (BCG)

INTRODUCTION

The situation surrounding COVID-19 is dynamic and rapidly evolving, with still unknown implications for the global economy and millions of human lives. No industry will be immune to the impacts of COVID-19, which will present both challenges and opportunities for businesses, particularly those with overseas operations. The crisis will likely have lasting impacts on how businesses operate and broadly play out over three phases – Flatten, Fight, and Future.

The Flatten phase, describing the stage when a nation or area is locked down in order to reduce the peak caseload, has prompted some businesses – particularly those providing essential services – to re-localise parts of their supply chain, building resilience ahead of a prolonged Fight phase. The Fight phase will see governments gradually ease restrictions with the aim of restoring a moderate amount of economic activity. While many businesses will be challenged during this period, it may also provide opportunities to prospective dealmakers, with BCG research showing that acquisitions executed in a weak economy tend to have higher returns than deals done in a strong economy.

When a vaccine or highly effective treatment eventually becomes widely available, we will transition to the Future phase. Economic activity will eventually be fully restored; however, it is likely some of the behavioural changes caused by COVID-19 will remain. For example, COVID-19's disruption to the status quo may make people more willing to engage remotely in the future, potentially providing new opportunities in established industries such as health and education services. At the time of publication, it is still too early to determine how COVID-19 will impact the overall trend of internationalisation seen among Australian companies in recent years.

SECTION SUMMARY

Australia's largest listed companies are becoming more internationally diversified, as measured by the proportion of revenue generated in foreign markets. ASX 200[29] companies generate 34 per cent of their revenues from foreign sources, more than the largest listed companies[30] in the UK (29 per cent) and US (26 per cent), but less than Japan (42 per cent).

The level of internationalisation seen among Australian companies differs meaningfully by sector. In some industries, such as utilities, insurance, consumer staples and banking, companies have tended towards less offshore expansion. Potential reasons include favourable local market dynamics, or offshore expansion being hindered by high barriers to entry or significant regulatory hurdles. By contrast, industries with favourable offshore market dynamics or high cross-border flexibility have an imperative to seek growth offshore. Mining, healthcare and IT are all export-heavy industries in which Australian companies continue to grow their offshore revenues at a higher rate than domestic revenues.

When considering larger ASX 200 companies ($2bn+ market cap), the incentives associated with offshore expansion are heightened when domestic growth opportunities are limited or constrained. Additionally, larger companies tend to be better equipped to navigate barriers associated with operating in a foreign market. It is then reasonable to expect that among the largest firms in a given market, higher international diversification would be associated with superior returns. This is demonstrated empirically among companies with $2bn+ market cap, by internationally diversified[31] companies outperforming domestically focused[32] companies on five-year total shareholder return (TSR).

While analysis of the complete ASX 200 dataset and previous academic studies[33] fail to reach a consensus on whether capital markets invariably support international diversification, they suggest that expanding offshore can be a valuable strategy under particular conditions. Like many strategic decisions faced by the board and management of Australian companies, there is no 'one size fits all' answer to offshore expansion. Expanding abroad can create significant shareholder value when compelling market conditions, strategic rationale and execution come together.

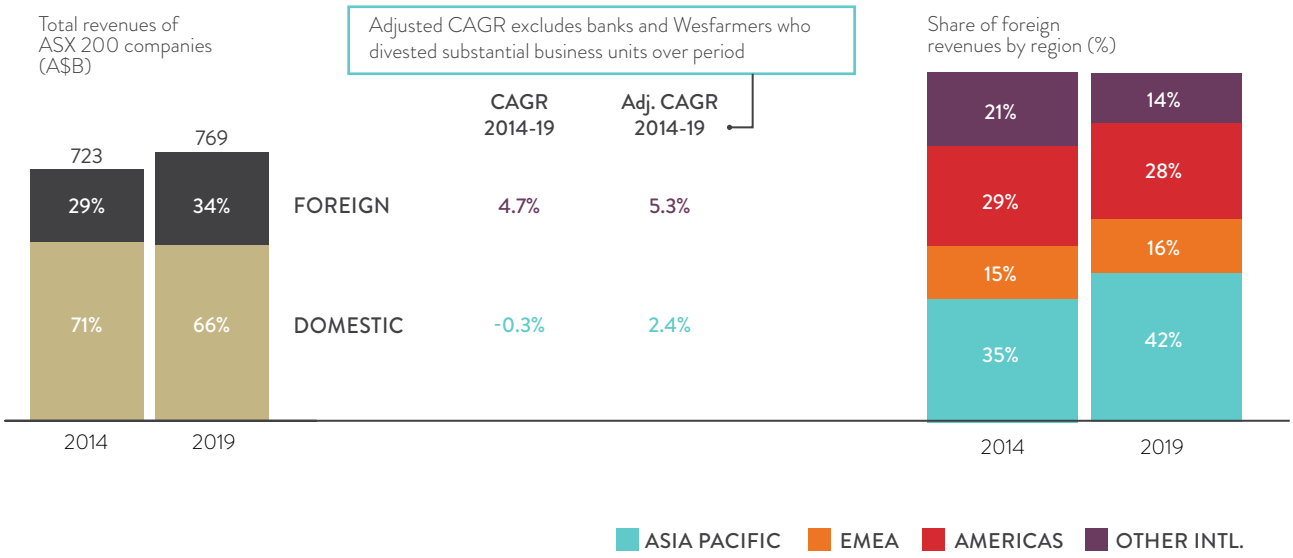
AUSTRALIA IS BECOMING MORE INTERNATIONALLY DIVERSIFIED

Over the last five years, as domestic growth plateaued, ASX 200 companies looked offshore for growth and to increase their exposure to foreign markets. The aggregate amount of foreign revenues generated by ASX 200 companies grew by 26 per cent from 2014 to 2019, while revenues from domestic sources were flat. As a result, 34 per cent of total revenues were generated from foreign sources in 2019, a five percentage point increase from 29 per cent in 2014.

Exports to the Asia-Pacific region in particular boomed over the last five years, growing at a rate of 8.5 per cent per year on the back of strong import demand for Australian goods and services from rapidly developing countries in the region. Exports by Australian companies to other regions of Europe and the Americas also grew, but at more subdued rates.

By contrast, the slight decrease in the ASX 200's aggregate domestic revenues from 2014 to 2019 can be explained by weak recent performance in the banking sector and significant divestments by a handful of the index's largest companies. The banking sector drove the decline in revenue due to unfavourable market conditions and the sale of a series of wealth management and insurance assets by the Big Four banks. Additionally, in the consumer sector, Wesfarmers' listing of Coles caused a (technical) reported loss of domestic revenues. Excluding these companies, the annual rate of growth in domestic revenues from 2014 to 2019 was positive at 2.4 per cent, but still slower than growth in revenues from foreign sources at 5.3 per cent.

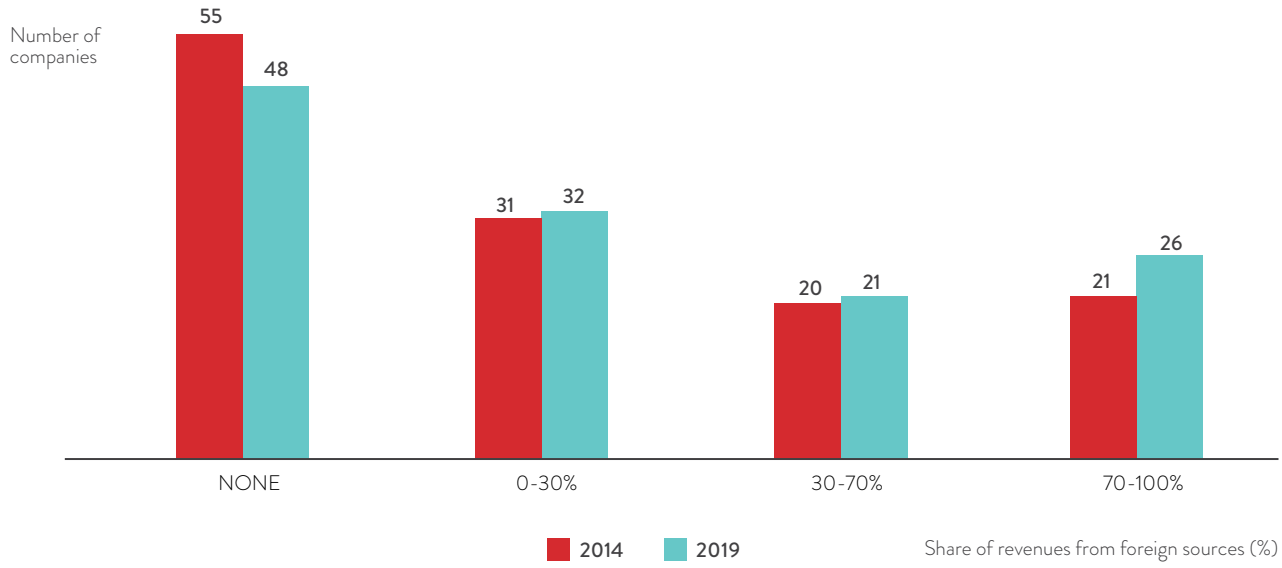
FIGURE 3. ***Share of revenues from foreign sources among ASX 200 companies has increased, driven by growing exports to Asia***



Note: ASX 200 dataset consists of 127 companies for which revenue by geographic region was available. Unspecified international revenues allocated to "Other International".
Source: S&P Capital IQ, BCG Analysis.

Comparing the distribution of companies by geographic revenue mix in 2014 and 2019, it becomes apparent that the growth in revenue from foreign sources was caused by an increase in both the number of companies exporting and the amount being exported by individual companies. From 2014 to 2019, the number of companies exporting increased by around 10 per cent, while five additional companies generated over 70 per cent of their revenues offshore.

FIGURE 4. ***More ASX 200 companies have begun to generate foreign revenues, particularly in the 70%+ range***



Note: ASX 200 dataset consists of 127 companies for which revenue by geographic region was available.
Source: S&P Capital IQ, BCG Analysis.

AUSTRALIA GENERATES A GREATER PROPORTION OF REVENUES FROM FOREIGN SOURCES THAN SEVERAL PEERS, DRIVEN BY EXPORTS FROM THE MINING SECTOR

Comparing Australia to global peers, the high proportion of revenues generated offshore in 2019 by ASX 200 companies (34 per cent) makes them more internationally diversified than the largest companies in the UK (29 per cent) and the US (26 per cent). Australia continues to trail Japan, however, where the largest companies generate 42 per cent of revenues offshore.

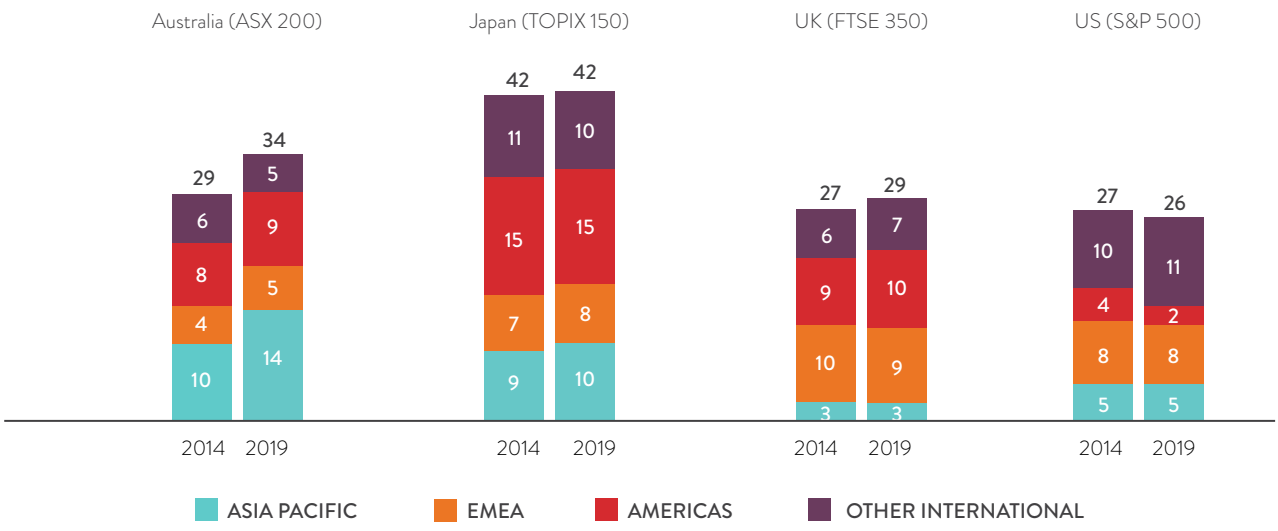
Australia's exposure to foreign markets has also grown at a faster rate than global peers, with a five percentage point increase in share of exports over the last five years, compared with a two percentage point increase in Europe and no change in Japan. By contrast, in the US, relative exposure to overseas markets reduced following recent protectionist policies and trade tensions between the US and China.

Australia's particularly strong growth was driven by increasing exposure to the Asia-Pacific region, now the highest of the global peer set despite Japan's geographic proximity. This is likely due to the different mix of goods and services exported – Australia's largest export products of minerals and raw materials are demanded predominantly by developing economies, of which there are many in the Asia-Pacific region. On the other hand, Japan's largest export products are high value-added, finished goods such as vehicles and machinery which are often sold to developed markets.

Considering the makeup of each country's exports by industry, over half of the ASX 200's foreign revenues are generated by the mining and materials sector. Conversely, in each of consumer staples, consumer discretionary, energy and industrials, ASX 200 companies generate the lowest proportion of total revenues offshore when compared with companies in the US, UK and Japan.

FIGURE 5. ***Japan has the highest proportion of international revenues amongst peers***

Proportion of total revenues by export region (2019, %)



Note: Analysis for companies where revenue by geographic region was available. (Japan: n=40, Australia: n=127, UK: n= 103, US: n=247); unspecified international revenues allocated to 'other international'. Figures may not add up due to rounding.
Source: S&P Capital IQ, BCG Analysis.

IN AUSTRALIA, INDUSTRY DYNAMICS HAVE SIGNIFICANT INFLUENCE ON THE DECISION TO EXPAND OVERSEAS

Among ASX 200 companies, there is considerable variation in the level of internationalisation by industry sector. Several industry-specific factors significantly influence management decisions to expand internationally – conditions in offshore markets relative to domestic markets, additional advantages from expansion of business offshore and ease of entering foreign markets, including regulatory barriers.

Firstly, companies operating in industries with slow domestic growth or high market saturation have reason to expand their operations offshore where market dynamics are more favourable. For example, Australia's rich supply of natural resources allows domestic mining companies to produce vast quantities of commodities that far outweigh local demand, given Australia's advanced economic development. To avoid a local supply glut and the resulting unfavourable conditions, miners look to sell their products in offshore markets with limited domestic production capacity.

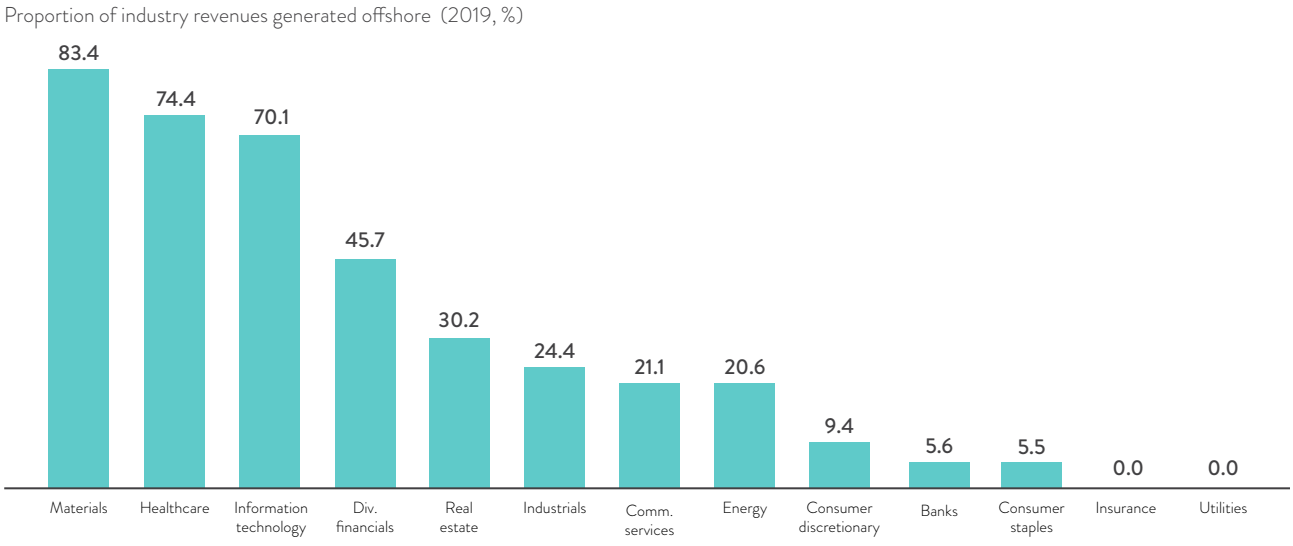
By contrast, Australia's consumer sectors have generally had favourable conditions relative to overseas markets, supported by a strong local economy which grew for 28 years without technical recession from 1991 to 2019. Additionally, offshore expansion in the industry remains particularly costly and risky, given that investment in a large network of stores is generally needed to compete with established local players, particularly in the grocery retailing subsector. As a result of unfavourable market dynamics and persistent risks associated with expansion, Australian retailers are provided less impetus to search for growth offshore. By continuing to focus on gaining a larger share of the Australian wallet, company returns in the S&P/ASX 200 consumer staples index have exceeded comparable benchmarks in the US, Europe and Asia over the last 10 years[34].

Secondly, in some cases the need to consider offshore expansion is heightened by other structural advantages, such as the opportunity to achieve economies of scale in sales volumes to overseas markets. This is particularly true for the medtech and biopharma subsectors of the healthcare industry, and for tech innovators, who need access to a global sales pool to recoup the considerable upfront investments required to develop intellectual property.

Lastly, industries with high levels of cross-border flexibility, including low levels of regulation, have lower incremental costs associated with offshore operation. The mining sector is an example of a market in which products are so commoditised that they are traded worldwide at a global price, which minimises the constraints of selling products offshore.

By contrast, banking and insurance companies often face significant barriers to offshore expansion as a result of low product flexibility and high levels of regulation, which increases the cost of establishing offshore operations. Australian banks ANZ and NAB have previously made significant efforts to expand into foreign markets and since largely retreated due to underperformance of their foreign assets, instead refocusing on core operations in Australia and New Zealand. In the utilities sector, stringent regulations on foreign ownership make it commonplace for companies to be restricted from entering offshore markets altogether.

FIGURE 6. ***Significant variation in level of international diversification between ASX 200 sectors***



Note: ASX 200 dataset consists of 127 companies for which revenue by geographic region was available.
Source: S&P Capital IQ, BCG Analysis.

LARGE COMPANIES THAT ARE INTERNATIONALLY DIVERSIFIED TEND TO OUTPERFORM THOSE THAT ARE DOMESTICALLY ORIENTED

There is evidence to suggest that, among larger companies, those that are internationally diversified create more value for shareholders than companies that are domestically focused. For the medium ($2bn-5bn) and large ($5bn+) market cap groups, the internationally diversified group outperformed the domestically focused group on average in long-term value creation, measured by a five-year TSR from 2014 to 2019. Internationally diversified companies in the medium group achieved on average 82 per cent more shareholder returns, while in the large group they achieved on average 36 per cent more shareholder returns.

This outperformance by large, internationally diversified companies generally holds within industries as well. Among medium and large companies ($2bn+), the internationally diversified group outperformed domestically focused companies on average five-year TSR from 2014 to 2019 in all industries except industrials and IT[35].

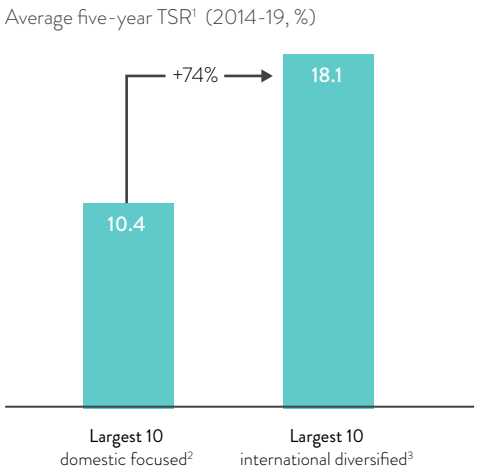
The relationship between international diversification and TSR is exacerbated when looking across industries at only the very largest companies in the ASX 200 by market cap. Among the 10 largest companies in each group, accounting for more than 70 per cent of ASX 200 market cap, those that are internationally diversified achieved on average 74 per cent greater shareholder return compared to those that are domestically focused, from 2014 to 2019.

As companies increase in size, some of the factors discussed in **'Australia generates a greater proportion of revenues from foreign sources than several peers, driven by exports from the mining sector'** – conditions in offshore markets relative to domestic markets and ease of executing offshore expansion – tend to skew in favour of offshore expansion. Indeed, larger companies often have a higher incentive to expand offshore as well as a greater ability to do so. As a company operating only in a domestic market grows larger, it is more likely to become constrained by domestic demand, which makes foreign markets increasingly attractive. Furthermore, larger companies are typically better resourced and equipped to navigate the challenges associated with offshore expansion.

FIGURE 7. ***For companies >$2B market cap, internationally diversified companies tend to outperform domestic companies on TSR***

1. Companies with >10% share of foreign revenues (n=51). **2.** Companies with <10% share of foreign revenues (n=60).
Note: Excludes companies not listed for at least five years.
Source: S&P Capital IQ, BCG Analysis.

FIGURE 8. ***Sampling the largest 10 companies of each group (>70% of market cap) shows large discrepancies in TSR results***



Largest dom. group constituents	TSR	Largest int. group constituents	TSR
CBA	7.2	BHP	8.7
Westpac	4.8	CSL	27.7
NAB	6.7	Rio Tinto Group	15.8
Woolworths	5.6	ANZ	4.4
Wesfarmers	11.7	Macquarie Group	23.9
Telstra	(2.3)	Goodman Group	26.3
Transurban Group	19.3	Newcrest Mining	27.8
Scentre Group	9.2	Sonic Healthcare	13.7
Sydney Airport	19.1	Brambles	6.5
ASX Limited	22.7	Xero	26.6

1. TSR runs 30 September 2014 - 30 September 2019. **2.** Companies with <10% share of foreign revenues. **3.** Companies with >10% share of foreign revenues
Source: S&P Capital IQ, BCG Analysis.

CASE STUDY

– GOODMAN GROUP

Goodman Group (GMG) is the most internationally diversified real estate company in the ASX 200 (measured by proportion of foreign revenues) and provides an example of how exposure to foreign markets allows a company to outperform domestic players on returns.

GMG generated 65 per cent of its revenues from foreign sources in 2019 following recent offshore expansion, particularly in Asia. The broader real estate index generates an average of only nine per cent of its revenues internationally.

While revenues from GMG's domestic business grew in line with the median rate of the industry index from 2014 to 2019, at seven per cent per year, offshore revenues grew approximately twice as fast at 15 per cent per year. GMG was able to capitalise on this to report a five-year TSR of 26.3 per cent, double the industry index return of 13.1 per cent.

THERE IS NO UNIFORM ANSWER TO OFFSHORE EXPANSION – IT REQUIRES SOUND STRATEGIC RATIONALE SUPPORTED BY STRONG EXECUTION

As discussed in previous sections, ASX 200 companies are exposed to varying market dynamics which provide the board and management of each company with a unique set of opportunities and challenges to consider when making strategic decisions on growth. As a result, there is no 'one size fits all' answer to international expansion; business leaders should assess geographic expansion against other growth opportunities on a case-by-case basis.

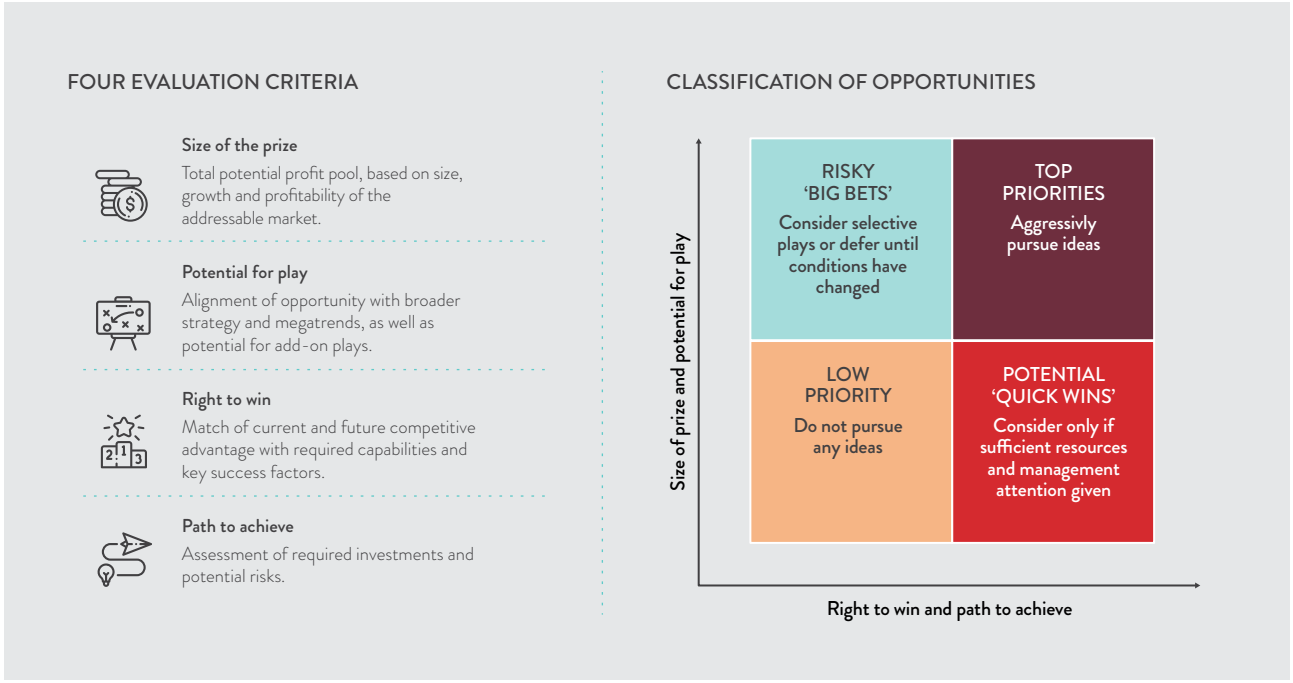
This observation is supported by analysis of the complete ASX 200 dataset which finds no uniform relationship between a company's geographic revenue mix and their TSR[36]. This is reaffirmed by a review of related literature which is similarly unable to determine if capital markets are invariably supportive or discouraging of international expansion.

A review of literature[37] reports mixed results:

- A study of European firms suggests capital markets are unsupportive of international expansion, reporting that firms which acquire cross-border targets have lower abnormal returns than those acquiring domestic targets.
- A study of foreign direct investments by UK firms into emerging economies indicated markets are positively receptive to offshore expansions, with shareholders seeing significant wealth gains during the announcement period.
- A study of US companies proposed an inverted U-shape relationship between return on capital and degree of internationalisation, suggesting there is an optimal degree of internationalisation.

BCG takes the view that geographic expansion is one of a range of strategies that business leaders should consider when aiming to achieve growth in adjacent or new markets. Geographic expansion in a particular market, along with other growth opportunities identified by the business (for example, mergers and acquisitions-led growth, innovation, digital growth, etc), should be evaluated by management and prioritised accordingly. BCG suggests a decision-making framework that prioritises growth opportunities based on four criteria – size of the prize, potential for play, right to win, and path to achieve.

FIGURE 9. *Four evaluation criteria for prioritisation of growth opportunities*



Expanding abroad, like any growth strategy, can create significant shareholder value when compelling market conditions, strategic rationale and execution come together.

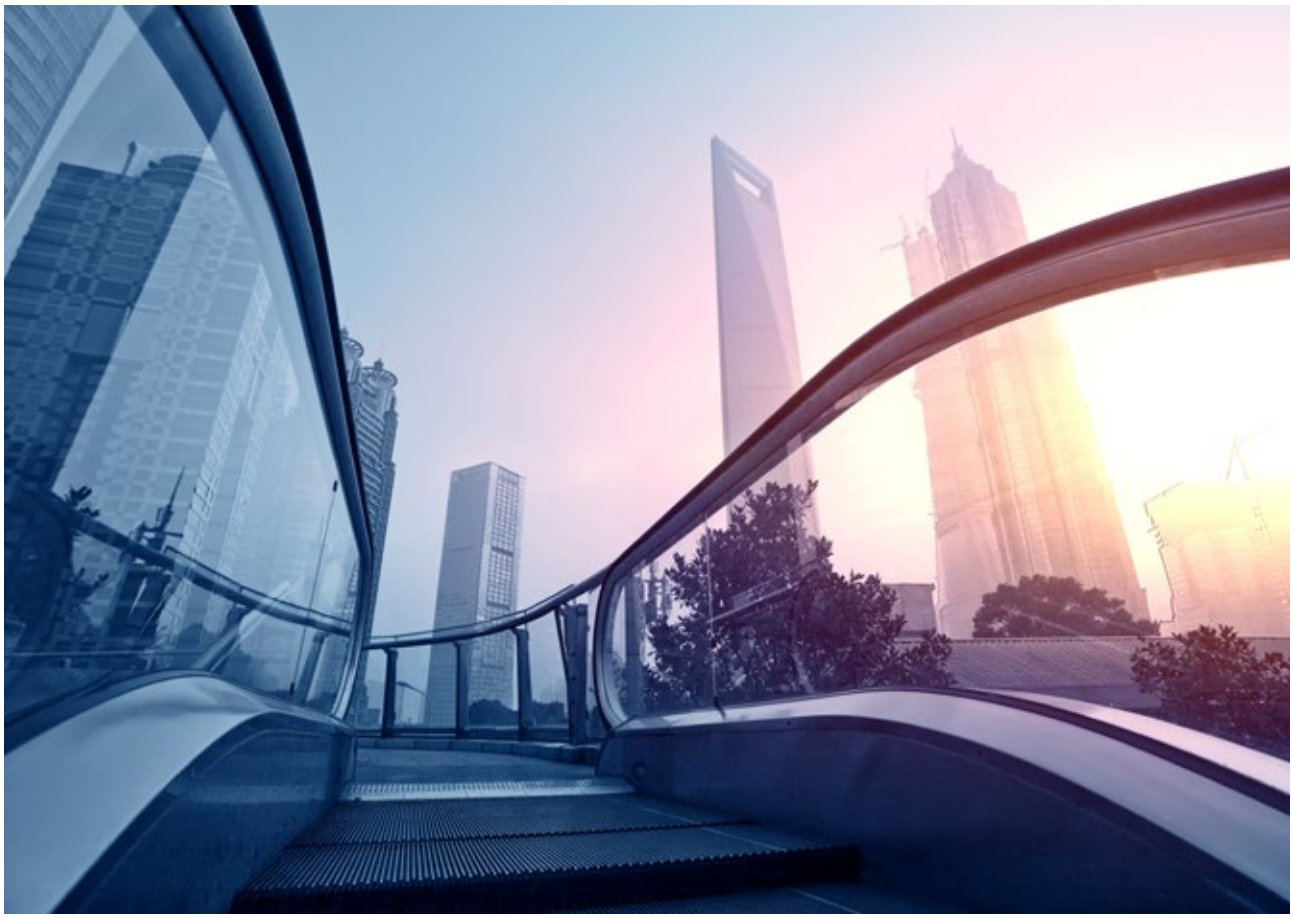
How the best ‘win in Asia’: Business models from companies succeeding in Asian markets

HOW THE BEST 'WIN IN ASIA': BUSINESS MODELS FROM COMPANIES SUCCEEDING IN ASIAN MARKETS

Part A (China) By Qiao Ma, Portfolio Manager – Asian Equities Fund, Cooper Investors;

Part A (India) By Mary Manning, Portfolio Manager for the Ellerston Asia Growth Fund, Ellerston Asian Investments (ASX:EAI) and the Ellerston India Fund, Ellerston Capital; and

Part B (Australian company case studies) by Mukund Narayanamurti, Chief Executive Officer, Asialink Business



INTRODUCTION

The previous section on **'Does offshore expansion lead to superior returns?'** highlighted critical factors that must be considered when undertaking international expansion. There is clearly no single factor that drives superior returns from international expansion.

Our extensive consultations have highlighted three major constraints currently impacting the internationalisation of Australian companies:

- The extensive use by senior leaders (boards and C-suite executives) of outdated anecdotes and examples of failures in Asian markets;
- The extensive use of media reports to inform views on strategies adopted by Australian and non-Australian companies in Asian markets; and
- A lack of substantive understanding of how market entry strategies and organisational capabilities determine success in Asian markets.

This section shares best practice business models for succeeding in Asian markets. The section is structured in two parts.

Part A: This part includes an analysis of non-Australian companies that have succeeded in China and India. The purpose of this category of case studies is for Australian companies to learn from international best practice in entering these highly competitive markets and generate market share, profitability and returns. We have identified these two markets as focus markets for two main reasons:

- China is Australia's largest trading partner and offers some of the most significant market opportunities for Australian value-added products and services. While there is public discussion in Australia on the need for trade and market diversification strategies, we believe that China will continue to be our largest trading partner for the foreseeable future. We also believe that there remain significant untapped opportunities for Australian companies with China's consumer class. For instance, the growing importance of the China International Import Expo (CIIE) to governments and companies internationally is an example of the extraordinary competition in the Chinese market for a share-of-wallet of the Chinese consumer. Understanding the strategies adopted by the most successful consumer companies in China (both local and foreign) will be particularly helpful for Australian companies.
- India has been identified by both business and government as critical to firm-level growth strategies. The India Economic Strategy to 2035 (IES) recognises that no other market offers Australia as much opportunity. A significant focus of the IES is growing outbound investment from Australia into India, an area in which there is currently a gap in understanding in corporate Australia – that is, how to invest in India, where to invest, and business and operating models to execute outbound investments effectively. The analysis on India focuses on addressing this gap.

We have included 14 case studies in this category of non-Australian companies that have succeeded in China and India.

Part B: This part includes an analysis of Australian companies across sectors that have successfully entered Asian markets. This includes:

- Case studies across technology, construction, property and infrastructure, healthcare, consumer staples, consumer discretionary, and financial services. These aim to give Australian companies a new reference point of best-in-class peers who have succeeded in Asian markets. We have included a combination of public companies and private companies. In respect of public companies, we have also included commentary on best practice in investor relations.
- A range of markets have been considered including China, Hong Kong, India, the Republic of Korea (South Korea), Singapore, Malaysia, Vietnam, Indonesia and Japan.
- All case studies were developed in collaboration with CEOs, CFOs or senior executives of the companies profiled.

We have included eight detailed case studies in this part.

WHAT DO WE MEAN BY BUSINESS MODELS?

Too often analysis of business models reduces to a discussion of the mechanisms or entry modes to execute a strategy, which include:

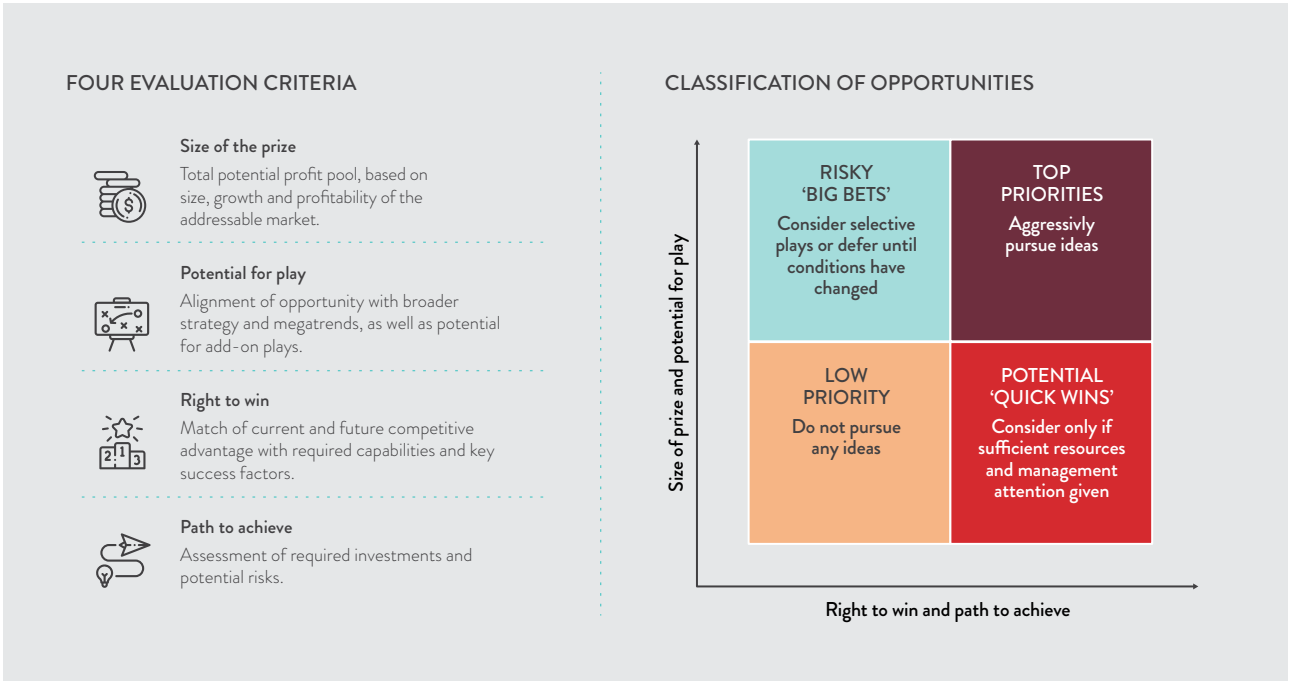
- Agent/distributor
- E-commerce
- Licensing
- Strategic alliances
- Corporate venture capital
- Wholly owned subsidiary
- Joint venture (JV)
- Mergers and acquisitions (M&A)
- Listing in host country.

Clearly, these entry modes differ depending on the host market, regulatory requirements, sector, availability of capital and so on. However, what is often missing from the discussion is a set of criteria for evaluating opportunities and a capabilities framework to execute confidently. Modes of entry follow as a third – and not first – layer of determining business models. The case studies in this section highlight the sophisticated consideration of criteria to expand offshore and the high level of individual and organisational capabilities required to execute.

The companies profiled as case studies use a breadth of entry modes from distributors and wholly-owned subsidiaries to JVs and M&A.

Both parts A and B aim to reflect all the elements that comprise a comprehensive approach to developing and executing business models in Asian markets: the four evaluation criteria for prioritisation of growth opportunities, the 11 Asia capabilities and the modes of entry.

FIGURE 10. *Four evaluation criteria for prioritisation of growth opportunities*



Source: BCG.

TABLE 1. *The 11 Asia capabilities*

INDIVIDUAL CAPABILITIES	ORGANISATIONAL CAPABILITIES
Sophisticated knowledge of Asian markets/environments	Leadership committed to an Asia-focused strategy
Extensive operating experience in Asia	Customised Asian talent management
Long-term trusted Asian relationships	Customised offering/value proposition based on customer insights
Ability to adapt behaviour to Asian cultural contexts	Tailored organisational design with tendency towards local autonomy
Capacity to deal with government	Supportive processes to share Asian learnings
Useful level of language proficiency	

Source: Asialink Business

FIGURE 11. *Modes of entry*

PART A: THE JOURNEY OF DOMESTIC BRANDS IN CHINA AND WHAT THIS MEANS FOR AUSTRALIAN INDUSTRY LEADERS

By Qiao Ma, Portfolio Manager – Asian Equities Fund, Cooper Investors

COVID-19 AND CHINESE COMPANIES

China went through a full cycle of widespread virus, hard lockdown, stabilisation and recovery from February to June 2020.

While the short-term pain was felt by all companies, we observed drastically different performances between industries, and between companies in the same industry. The strong companies became stronger and emerged out of COVID-19 with an even more superior industry positioning.

Proprietorial culture, where management acts and thinks like owners, proved to be an effective antidote to systemic shocks. Resilience is a core tenet of proprietorial culture. These founders and CEOs, having built the businesses from the ground up and navigated through myriad competitive and regulatory challenges, did not flinch in the face of crisis. They wasted no time complaining or waiting for help from the government. They worked through the Chinese New Year holidays side-by-side with frontline employees. They ensured that their employees stayed healthy, created innovative solutions to meet customer demand and resumed business quickly when it was safe.

Consider Shenzhou, the leading global sportswear manufacturer, as an example. Mr Ma Jianrong, Shenzhou's founder and CEO, started working at a Chinese textile factory at the age of 13. A few months of national lockdown was not going to cause Mr Ma to panic. Shenzhou quickly ramped up its compliance and safety procedures and was among the first businesses to be given a permit to re-open in mid-February. When other textile factories scrambled to find workers and face masks (a work condition requirement), Shenzhou calmly sent out buses to ferry its 17,000 workers from 17 provinces back to its Ningbo factory. Bear in mind that during that time, provincial borders were closed. To be able to fetch the workers means Shenzhou had cleared bureaucratic obstacles to cross 17 provincial borders beforehand. Mr Ma also had the foresight of building vertical supply chains within each country where Shenzhou operates. As a result, its Chinese factory did not need to wait for fabric from Cambodia, and vice versa. There is confidence that global sportswear demand will normalise over time, and companies like Shenzhou will emerge as a strong market share gainer.

Observing the Chinese companies through the crisis also enhances our conviction in the long-term thesis on investing in Asia – many Asian businesses have become truly best-in-class operators in their fields. Their maturity in managing inventory, staff and customers in times of crisis rivals any large multinational.

China Mengniu, a leading dairy company, is a good example. As shops were closed during COVID-19, Mengniu's sales teams quickly pivoted to e-commerce and other ways of engaging with customers directly. They set up more than 90,000 WeChat groups, and sales from these community marketing efforts reached 10 per cent of revenues in the March quarter. Mengniu is also proactive in inventory management. Its points-of-sale system identified unsold inventory in traditional small retail outlets due to store closures. It quickly bought back these inventories and sold them via modern retail or online channels. Mengniu's Environmental, Social and Governance (ESG) team also kicked into full gear, transporting large quantities of milk and yoghurt to hospitals in need. Mengniu is emerging out of the crisis with a solid inventory position, a nimbler and more capable sales team, and higher brand recognition.

Another clear trend that we have observed in China is the elevated importance of IT. During COVID-19, IT became essential for survival. Whether a company has resilient IT infrastructure, and more importantly, the right *technology culture* where employees create and embrace new solutions, means the difference between business largely-as-usual and complete shutdown. Examples of these companies with leading IT solutions in their respective industries, and who enjoyed markedly better operating trends than their peers, include:

- YUMC championed 'contactless deliveries' in early February. Food goes from the kitchen to consumers without human touch. Its booming online business helped cushion restaurant closures and maintain engagement with customers. This practice has since been emulated by delivery platforms and quick-service restaurants globally.
- Sun Art's investments in online delivery over the past two years paid off handsomely. Its online grocery deliveries saw a spike in demand and more importantly, operations went smoothly to meet sudden demand surges.
- Ping An's agents (insurance) continue to conduct many business functions online, including the signing up of new customers.

Introduction

The evolution of domestic Chinese companies over recent decades in competition with foreign multinationals is one of the more fascinating aspects of China's economic rise.

It is a story of transformation and also shines a light on just how intense competition is in virtually every aspect of business within an economy that remains on track to have doubled in size over the past decade.

By examining this phenomenon, we gain insights into both success and failure and develop learnings about what is required in order to be truly competitive in the Chinese market.

To properly understand the dynamic nature of China's economy today – increasingly consumer-led by a 400 million-strong middle class – and the interplay between local companies and foreign multinationals, it pays to look back to 1978, when Deng Xiaoping announced the 'open door' policy that paved the way for the progressive opening of the Chinese market to foreign business and investment.

This was a time when there was virtually no foreign brand recognition or familiarity among the Chinese population. The market was dominated by state-owned enterprises (SOEs) with no competition and therefore no imperative to evolve or innovate. Over the next two decades, however, China saw waves of foreign companies enter and corner the premium ends of the domestic market, by capturing the imagination of Chinese consumers.

This foreign dominance was widespread in everything from sports shoes and clothing to beauty products and even toothpaste. The product quality, all the way through to packaging, was considered so far and away superior to local alternatives by consumers that foreign brands generally did not even need to tailor their brands or marketing campaigns for the Chinese market. The items virtually sold themselves.

For example, Nike, which first entered the Chinese market in 1981, did not feel the need to have targeted advertisements for local consumers until the Beijing Olympics of 2008.

As foreign companies largely competed among themselves to increase market share across most categories, various high-profile product scandals and controversies involving local Chinese companies only exacerbated a crisis of trust in local brands.

CASE STUDY

SHIJIAZHUANG SANLU GROUP: CONTAMINATED INFANT FORMULA

In September 2008, it was discovered that a group of Chinese domestic dairy companies, most notably the Shijiazhuang Sanlu Group, had produced and sold infant formula contaminated with high levels of the industrial chemical melamine.

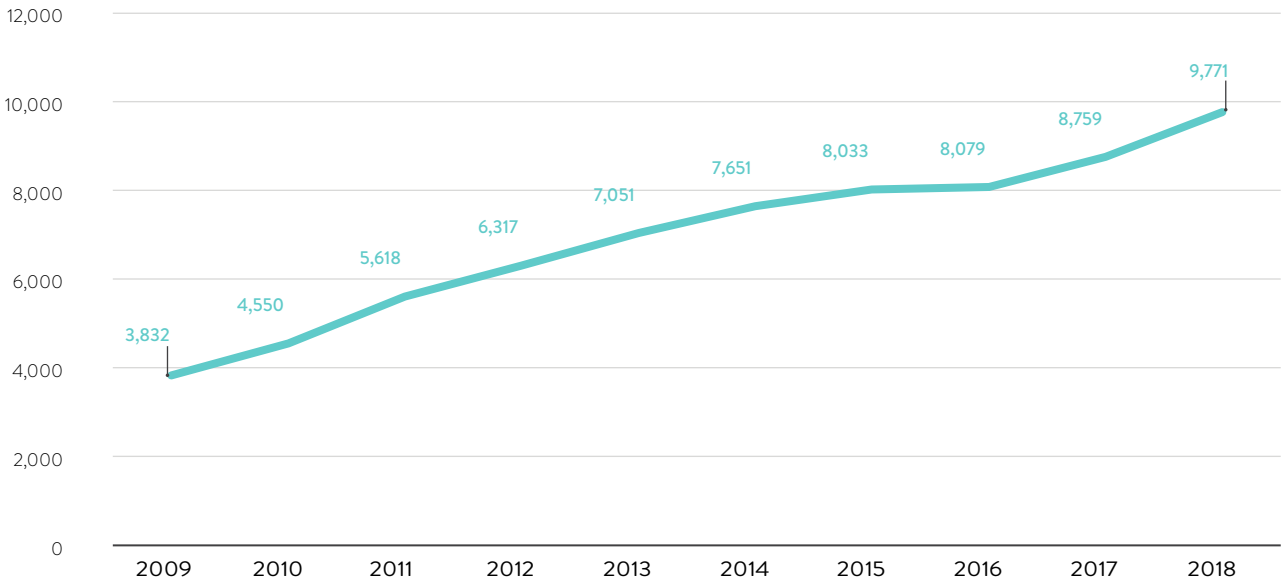
Almost 300,000 children were estimated to have become ill, while six infant deaths were linked to the contamination. Sanlu Group went bankrupt as a result, while the former chairwoman received a life sentence and others received death penalties.

The scandal and its cover-up destroyed consumer confidence in the domestic infant formula industry for a decade. The market share of domestic local companies plummeted as consumers turned to more trusted imported products.

China's consumption upgrade

Over the past two decades, China has experienced a progressive 'consumption upgrade' as rising incomes afford consumers increasing levels of choice. This has resulted in a significant shift in consumer attitudes, with significant numbers of Chinese consumers becoming more discerning and therefore prepared to pay higher and premium prices for products and services that they consider enhance their quality of life.

FIGURE 12. ***China GDP per capita 10-year trend (US$)***



Source: World Bank

This major shift in consumer attitudes has had a profound impact on business psychology. For example, domestic companies, including manufacturers, are no longer focusing exclusively on producing and selling items at the lowest cost. Instead, many local companies have pivoted to produce higher-quality goods and services, but as efficiently as possible.

As state ownership of companies has receded, entrepreneurialism and innovation have flourished. The founders and managers of many 21st century Chinese businesses have different mindsets, skills and experiences to the flat-footed operators of the old-style SOEs. Many Chinese who have started businesses in the modern era have gained experience working in foreign companies, including multinationals. They are tech-savvy, well-travelled and in many cases highly educated, having acquired qualifications from leading overseas universities.

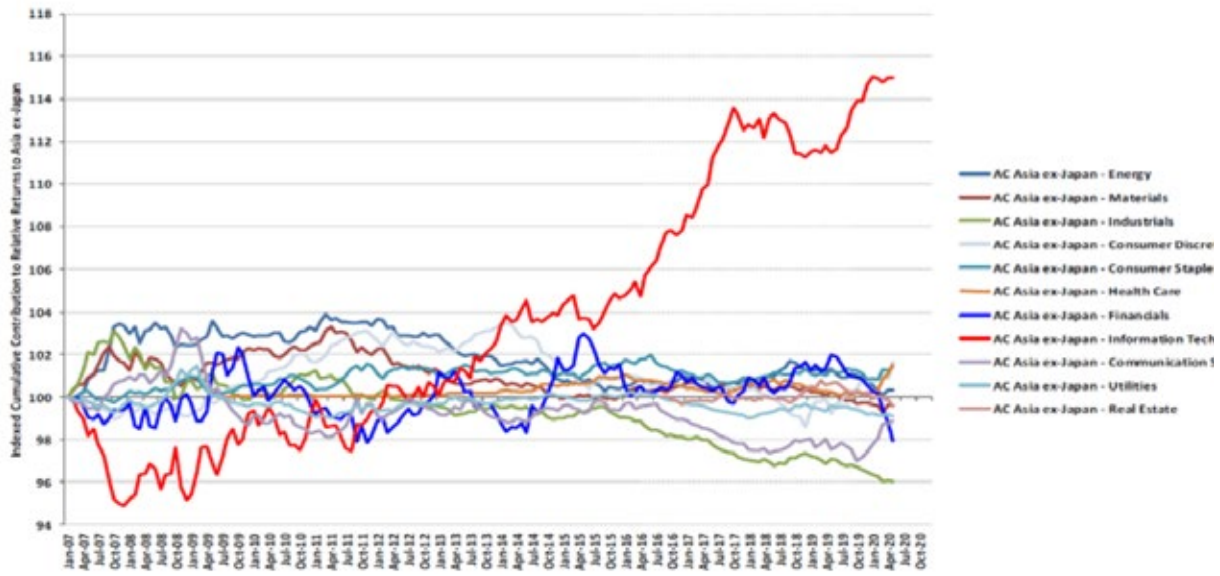
Many are in a hurry; they are quick learners and have combined the lessons of working in other companies with their own local market knowledge and entrepreneurial spirit to become formidable operators of their own businesses.

The rise of the internet

The rise of the internet and e-commerce in China has also been a major transformative market force. In the decade between 2005 and 2015, China's digital companies formed the nation's largest industry, surging past the likes of energy and industrials. These companies now account for more than one third of China's total market capitalisation.

The rise of internet companies has not only produced global household names such as Jack Ma but has cross-pollinated with other sectors such as discretionary retail, as a powerful enabler of innovation and sales growth.

FIGURE 13. ***Sectors' indexed cumulative sector contribution to relative return to Asia ex-Japan***



Source: BofA Asia Pac Quantitative Strategy, IBES, MSCI

This intersection has also seen the movement of talent from technology companies into senior positions within traditional businesses.

For example, one of insurance and financial services giant Ping An's three CEOs, Jessica Tan, brought with her a technology background as fintech specialist with global consulting firm McKinsey & Company, while Yum China, which operates KFC and Pizza Hut in China, promoted two key talents from its IT department to general managers of the flagship brands. These progressive and highly capable individuals have become catalysts for change in these businesses and have elevated the role of technology internally.

Cultural change in business

The cultural change that continues to sweep through many traditional Chinese businesses is profound. Younger tech-savvy employees are being promoted into newly created and important roles. Large and cumbersome bureaucratic business functions have been replaced by small, agile, project-based teams with specific missions and KPIs, while instinctual and experience-based decision-making has been supplemented or in some cases replaced by data-based thinking.

Business processes have been accelerated and product innovation cycles shortened. Large-scale product launches promoted by traditional media were considered crucial to marketing success in the past. Today, consumers are within constant reach via online channels and companies with brand recognition and consumer trust are more focused on making small, iterative improvements to their goods and services in order to gain a competitive edge. The frequent and seemingly minor upgrades to Apple products highlight this approach, which consumers expect and demand.

A high level of cultural tolerance for failure has also developed, helping to further drive innovation and risk-taking at every level. KFC China, for example, is known to add more than 100 new items to its menu each year, while replacing other items that are not resonating with its customers.

Domestic companies are also producing not only higher-quality products but also creating attractive, original designs.

CASE STUDY

LI-NING RISES AGAIN

World champion gymnast Li Ning became a national hero in China after winning six medals, including three golds, at the 1984 Olympic Games.

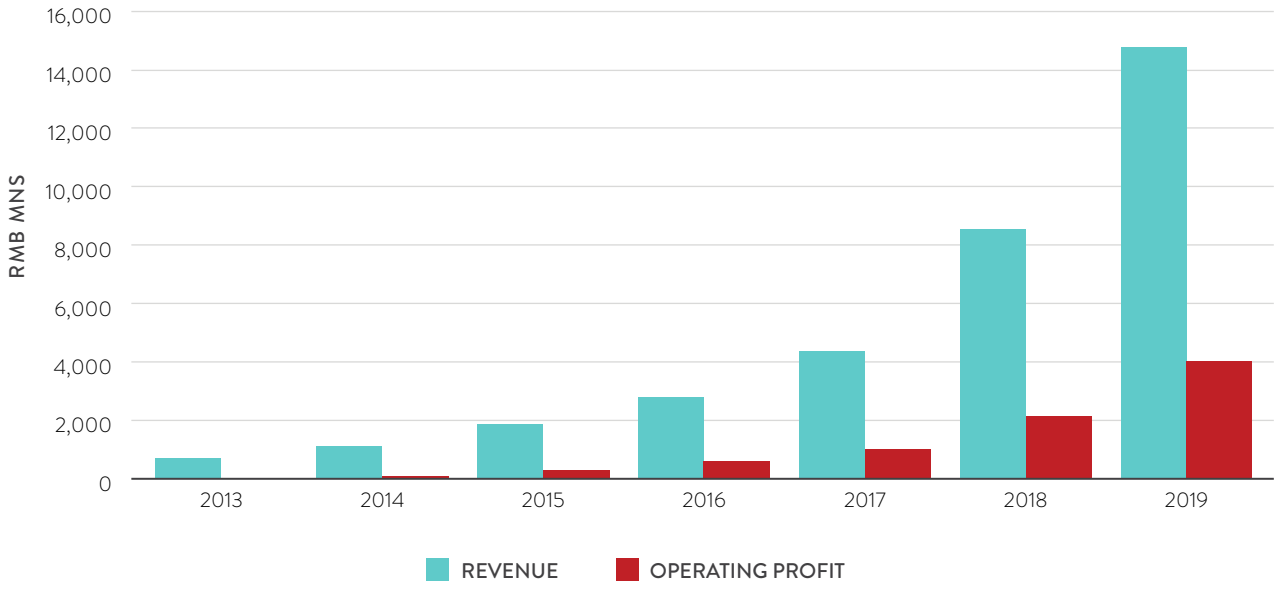
On retirement, he founded a sporting footwear and apparel company in his name (Li-Ning). Riding on the wave of Li Ning's popularity, the company enjoyed a decade of success before ceding ground to the likes of Nike and Adidas. In 2018, the company responded to the challenge with the release of a striking new range of casual sportswear – 'China Li Ning' – which was unveiled at New York Fashion Week. The new designs, including 'on-trend' footwear, successfully tapped into China's nationalistic spirit and sense of nostalgia, catapulting Li-Ning back to being one of the most popular sporting brands in the country. Li Ning remains company chairman to this day.

Acquiring international brands

Over the past decade, Chinese companies have also become increasingly proactive in acquiring established international brands – a strategy that removes the need to establish new brands and products and then endure the long time required to gain recognition and consumer confidence.

Often these acquisitions are value-accretive and have turned foreign brands that are relatively small, but which have market recognition, into major domestic franchises. For example, Anta, a successful Chinese sportswear company, acquired the exclusive local rights for the fading Italian heritage sports brand, Fila, in 2009. The Fila brand globally has since had something of a renaissance with a surge in popularity for retro sportswear and in China revenues and operating profits have grown over ten-fold over the past decade.

FIGURE 14. *Revenue and operating profit performance of Fila China*



Source: Anta's company filings and CI estimates

Fuelled by the success of Fila, Anta went on to acquire Finnish company Amer Sports in 2019 for a reported US$5.15 billion. Amer owns globally known brands, including Salomon, Arc'teryx, Peak Performance, Atomic, Suunto, Wilson and Precor.

As mentioned earlier, China's infant formula scandals destroyed confidence in local brands and Chinese dairy companies have spent several years trying to win back consumer confidence and market share. China Mengniu is one of China's largest domestic dairy companies and it was among the several companies implicated in the scandal. It is known for its high-profile marketing campaigns and has been able to regain confidence for producing quality products.

In 2019, China Mengniu acquired Australia's fourth-largest organic infant formula company, Bellamy's, for a reported AU$1.5 billion as well as another Australian company, Lion Dairy and Drinks, for a reported AU$600 million. These were considered smart acquisitions given the excellent reputation of Australian dairy products among Chinese consumers.

CASE STUDY

ASTROBABY: SUCCESS AFTER SCANDAL

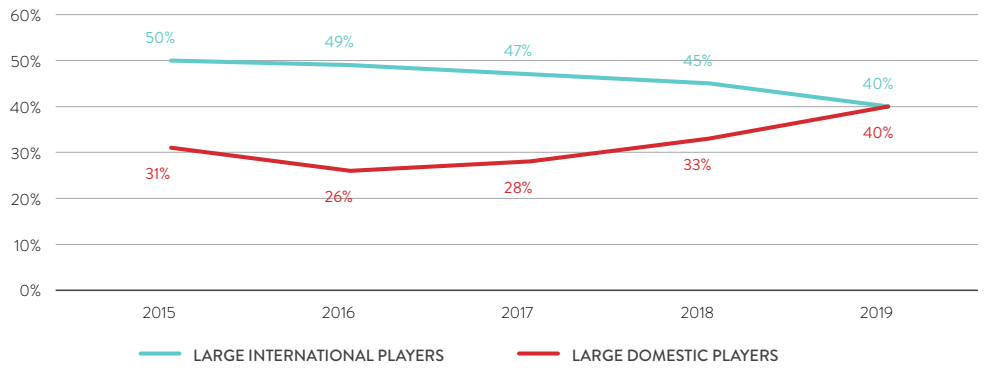
After losing market share to international companies for a decade, domestic infant formula companies started to recapture lost ground.

One company that stands out is Feihe. Its flagship product, Astrobaby, went from a largely unknown brand to the highest-grossing infant formula in China with almost US$1 billion in annual sales.

Unlike many competitors, Feihe does not source products from overseas – all products are sourced and processed strictly in China. Feihe has been able to successfully market its products as "most suitable to Chinese babies". It employs a team of 2,500 highly trained sales staff, who visit local mother-baby stores to provide advice and run frequent events. In 2018 alone, Feihe conducted 300,000 face-to-face events across 100,000 points of sale.

Feihe also employs a sophisticated digital system to ensure quality control. Each can of infant formula has a unique QR code which consumers scan to verify authenticity. Through its system, Feihe can also assess real-time inventory levels at local stores. It also engages with customers through the WeChat social media platform. Through the success of brands like Feihe, the overall market share in dairy for domestic brands has climbed back to 60 per cent as of 2019.

FIGURE 15. *International vs domestic offline infant formula market share in China*



Source: *Nielsen*

TABLE 2. *Comparison of offline infant milk formula market share by company in China in 2015 and 2019*

2015		2019	
Nestlé SA	12.9%	Nestlé	13.5%
Danone	6.3%	**Feihe International Inc**	**13.3%**
Abbott Laboratories	6.3%	Danone	10.1%
Mead Johnson	6.0%	Abbott Laboratories	6.7%
Yili	5.4%	Mead Johnson	6.1%
Feihe International Inc	**5.3%**	**Junlebao**	**5.5%**
Royal FrieslandCampina	4.9%	**Yili**	**5.3%**
Beingmate	**4.6%**	Royal FrieslandCampina	5.1%
Mengniu Dairy	**3.8%**	**Ausnutria**	**5.0%**
Health & Happiness	**3.5%**	**Health & Happiness**	**4.9%**

Source: Euromonitor Note: bold denotes domestic companies

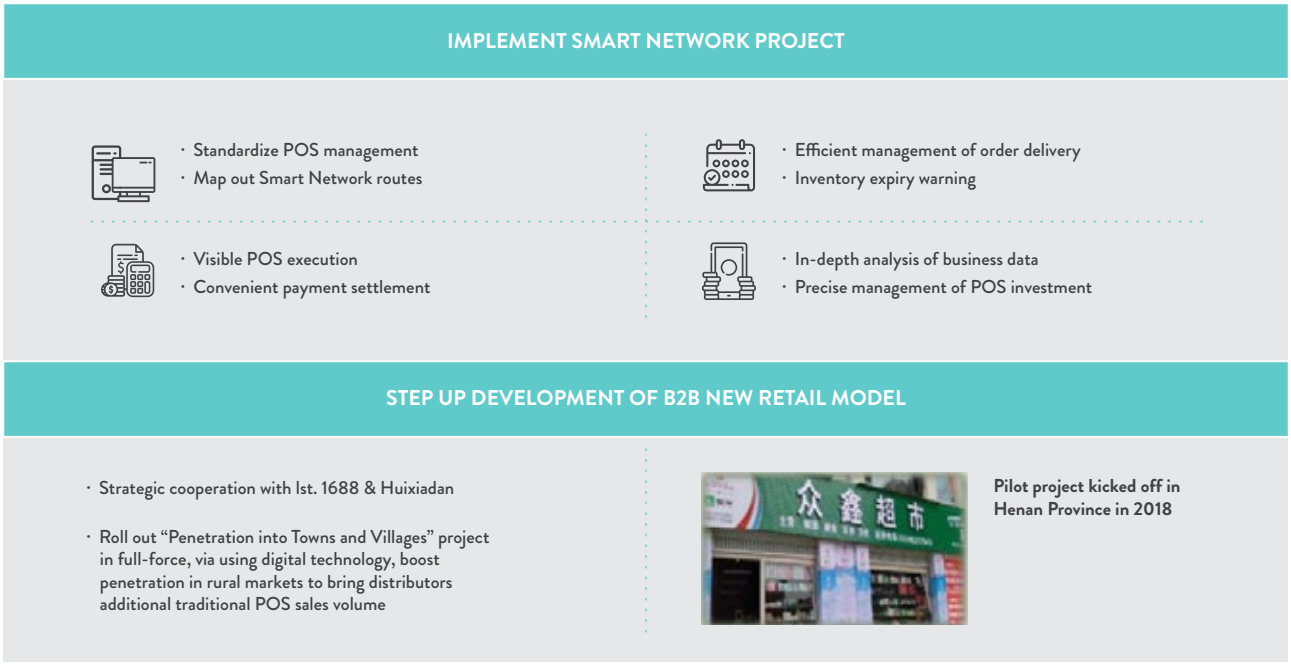
Marketing and distribution in China

Given the scale of the Chinese consumer market in terms of numbers, geographic spread and variance, local marketing and distribution is a traditional strength of many of China's domestic companies. This competitive advantage is magnified when combined with advanced digital capabilities. China is effectively divided into five Tier 1 cities, 30 Tier 2 cities, 60 Tier 3 cities and thousands of other smaller cities, towns and villages.

This is a vast and complex system that requires extremely large sales forces to physically cover and multi-tiered management structures to ensure consistent execution across the various markets. As a result, most foreign multinationals have rarely extended their footprint beyond the Tier 2 cities, whereas large local companies, with sales teams often exceeding 100,000 people, have been able to penetrate much deeper into different markets.

Advanced domestic companies have further upgraded their sales capability with the adoption of sophisticated digital point-of-sale (POS) and inventory management systems. Sales representatives can better target their efforts by utilising real-time sales information. China Mengniu, for example, operates a deep, national distribution network that covers 1.5 million points of sale which it is digitising through the rollout of a 'smart network' project. It is partnering with Alibaba in using its leading Ling Shou Tong retail inventory management platform to boost its market penetration.

FIGURE 16. *Keep enhancing sales capability – empower distributors*

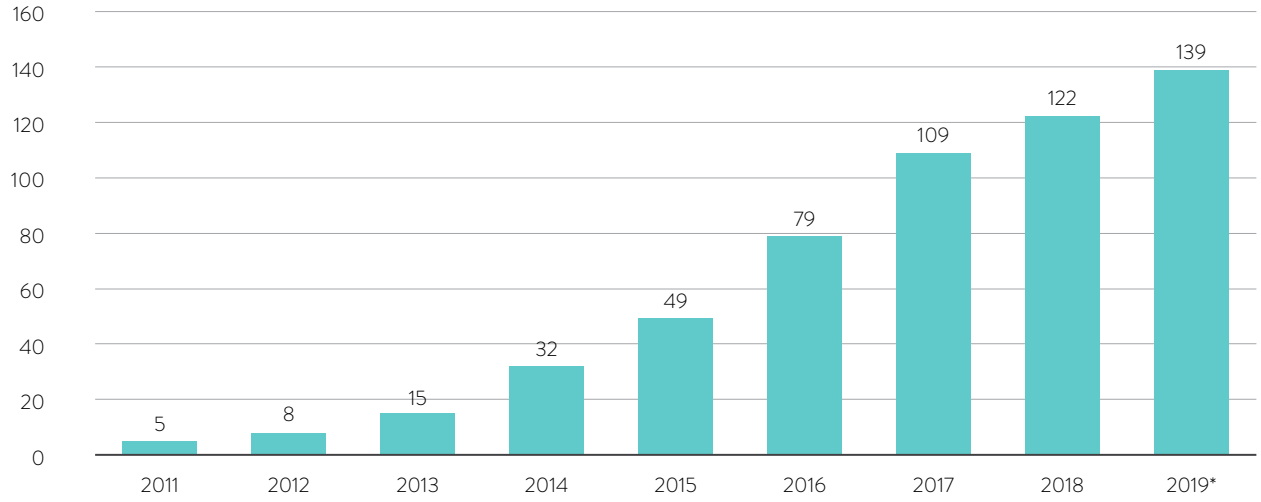


Source: Adapted from Mengniu investor presentation

The effective use of data

The sophisticated use of data in the Chinese market, including the ability to collect, interpret and analyse enormous volumes of data, affords local companies a further competitive advantage. Yum China, for example, describes itself as "an IT company that happens to be selling fried chicken and pizzas". It utilises industry-leading software to map out the most efficient delivery routes and can provide customers with personalised menu recommendations via digital channels. Similar characteristics can be observed in Huazhu Group, which operates more than 5,000 hotels and uses advanced digital technology to drive its automated check-in systems, patron membership/loyalty programs and service-tracking systems. Like Yum China, Huazhu Group is an IT company that also runs hotels.

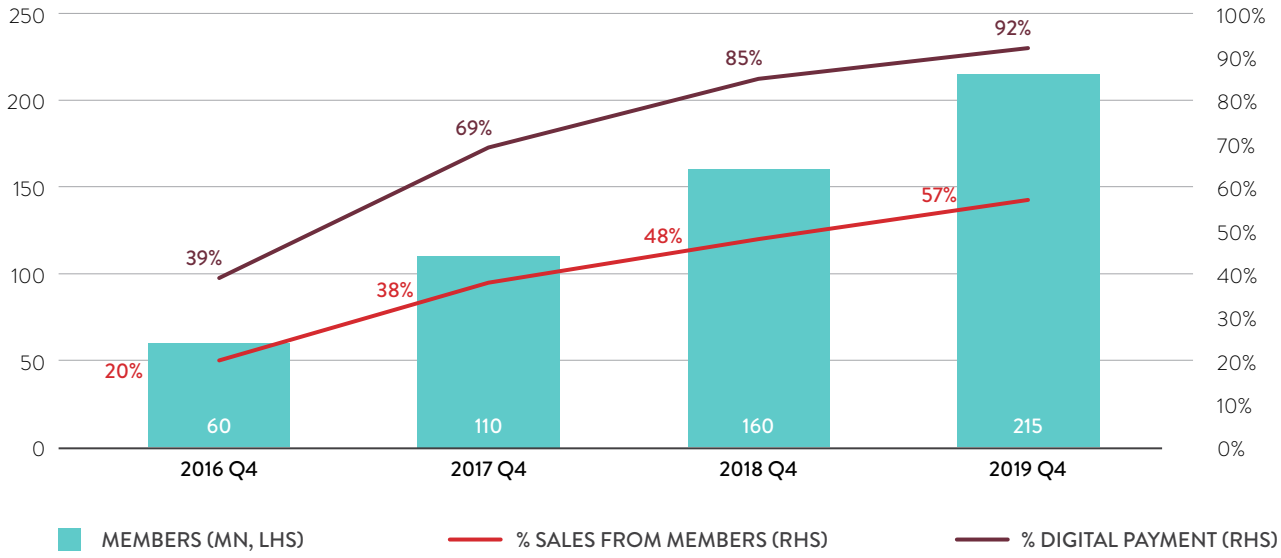
FIGURE 17. *Huazhu Group loyalty program members (MN)*



*As at September
Source: Huazhu Group investor material

More generally, big data will increasingly help companies to improve their personalised marketing efficiency and at the same time further build deeper levels of customer engagement and loyalty. Knowing your customers and what their preferences are will make costly, large-scale, blanket advertising campaigns largely redundant – replaced by targeted and personalised digital engagement. The effective use of data is also accelerating the development of products and services through the feeding of real-time consumer data into R&D processes.

FIGURE 18. *Percentage of sales and digital payments by KFC members in China*



Source: Yum China's investor material

Key learnings – how to succeed in China today

Fierce competition in every aspect of commerce is simply unavoidable when doing business in China.

It has been said that the only constant in China is that China is constantly changing. There is no single formula for success and China must not be viewed as one homogenous market – it is a multitude of markets, each with unique characteristics.

To adapt the famous quote of American abolitionist Wendall Phillips, "eternal vigilance is the price of liberty," it can be argued that "eternal vigilance is the price of commercial success in China and indeed Asia".

In hoping to compete, standing still is simply not an option. Agility is required and that means an ability to quickly adapt to market forces and change course if required. Innovation must be embraced at every turn and digital technology, including real-time data, effectively utilised.

Meaningful investment will be required, and foreign companies can no longer simply rely on their international reputations to win the day under an 'asset-light' business model. A sufficiently sized on-the-ground team, led by a manager who is digitally savvy and acts like a local business owner, are key to success.

Frequent changes in consumer preferences are also to be expected and this requires a flexible product development strategy and manufacturing capability.

Data from consumers should be treated like gold. The gap between companies that truly know their consumers and those that don't will grow ever larger. For example, the ability to set up and manage digital engagement channels, with the support of leading capability enablers such as Tencent, should be considered non-negotiable.

Finally, the importance of an entrepreneurial and proprietorial culture cannot be overemphasised.

Winning characteristics can be summarised as follows:

- Humility to learn from competitors, both at home and abroad, in areas such as product design, marketing strategy and quality control.
- Ability to quickly adapt to changes in consumer preferences.
- Willingness to take risks with a preparedness to invest in, test and utilise technology in all aspects of business.

In many respects, succeeding in China comes down to survival of the fittest. There is certainly truth in the adage "what doesn't kill you makes you stronger" – survivors that emerge successful in China are usually fiercely competitive and capable of succeeding anywhere.

Chinese companies such as Alibaba and Netease are rapidly gaining success in international markets and this is a trend that is definitely set to continue.

HOW THE BEST MULTINATIONALS INVEST IN INDIA AND DRIVE MARKET SHARE, PROFITABILITY AND RETURNS: LESSONS FOR AUSTRALIAN COMPANIES

By Mary Manning, Portfolio Manager for the Ellerston Asia Growth Fund, Ellerston Asian Investments (ASX:EAI) and the Ellerston India Fund, Ellerston Capital

Introduction

India is currently the world's fifth-largest economy with a GDP of over US$3 trillion. Given its growth trajectory, by 2030 India is expected to be third-largest economy in the world after China and the US. India is home to 1.3 billion people and has the largest cohort of millennials worldwide. By 2030, approximately one-fifth of the world's working age population will be Indian, and India is expected to have nearly a billion internet users. Many sectors such as financials, consumer, utilities, infrastructure and materials remain at penetration levels far below developed markets and other emerging markets such as China and Brazil.

Despite the size and scale of the Indian market, it remains largely ignored as a destination for foreign investment by Australian companies. In 2018, only about 0.6 per cent of Australian outbound investment was allocated to India, less than that allocated to countries such as Luxembourg, the Netherlands, Bermuda and Papua New Guinea[38].

India is unlike any other market in the world. It has 22 official languages, 29 states and seven territories. It has some of the largest metropolitan centres globally, including Mumbai and Delhi with populations of more than 18 million people each, yet over 60 per cent of the population remains in rural areas. Due to COVID-19, the United Nations estimates that over 100 million Indians could fall below the poverty line, yet India is also home to Asia's richest man, Mukesh Ambani, and has the fastest growing population of millionaires[39]. India is primarily a domestic demand economy, but there are a number of sectors, namely IT services and pharmaceuticals, that are world-leading exporters.

These paradoxes, coupled with the sheer size and level of complexity of the Indian economy, means that one size doesn't fit all when it comes to market entry strategies and operational success for foreign companies in the Indian market. The table below provides some examples of multinational companies (MNCs) that have successfully entered and thrived in India. These examples hail from multiple countries of domicile, cut across sectors and include a number of different business models.

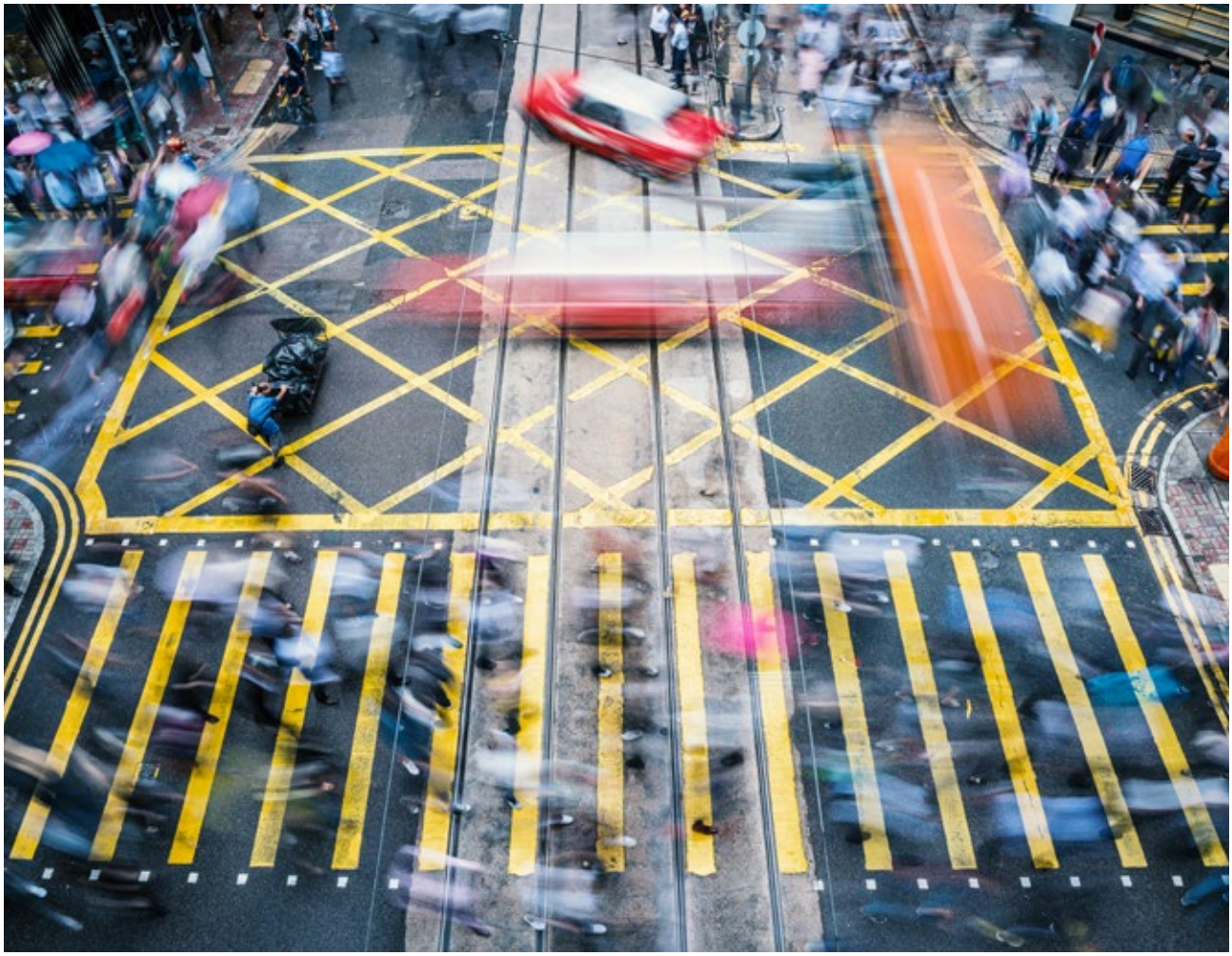


TABLE 3. *Multinational companies and their business model to enter India*

FOREIGN COMPANY	INDIAN COMPANY	DOMICILE OF FOREIGN COMPANY	SECTOR	STRATEGY
Unilever	Hindustan Unilever	UK/Netherlands	Consumer	Majority Stake
Nestle	Nestle India	Switzerland	Consumer	Majority Stake
Colgate Palmolive	Colgate India	USA	Consumer	Majority Stake
Suzuki	Maruti Suzuki	Japan	Autos	Majority Stake
Bayer	Bayer CropScience	Germany	Materials	Majority Stake
Cummins	Cummins India	USA	Industrials	Majority Stake
Kansai Paints	Kansai Nerolac	Japan	Industrials	Majority Stake
Abbott Laboratories	Abbott India	USA	Pharma	Majority Stake
Akzo Nobel	Akzo Nobel India	Switzerland	Industrials	Majority Stake
Fosun	Gland Pharmaceuticals	China	Pharma	Majority Stake
Bosch	Bosch India	Germany	Industrials	Majority Stake
Siemens	Siemens India	Germany	Industrials	Majority Stake
British American Tobacco	ITC	UK	Consumer	Minority Stake
Prudential Life Insurance	ICICI Prudential	UK	Financials	Minority Stake
Standard Life Insurance	HDFC Standard Life	UK	Financials	Minority Stake
Facebook	Jio Platform (Reliance)	USA	Technology	Minority Stake in Assets
Saudi Aramco	Reliance Refining Assets	Saudi Arabia	Energy	Minority Stake in Assets
Alibaba/Ant Financial / Softbank	PayTM	China / Japan	FinTech	VC Investment
PEPSI	Varun Beverages	USA	Consumer	Distribution Agreement
H&M and Zara	Arvind	Sweden/Spain	Retail	Distribution Agreement
Domino's Pizza	Juliant Foodworks	USA	Consumer	Franchise Agreement
McDonalds	Westlife	USA	Consumer	Franchise Agreement
7-Eleven	Future Group	USA	Retail	Franchise Agreement
Best Western	Cabana Hotel Management	USA	Hospitality	Franchise Agreement
Total SA	Adani Gas	France	Energy	Joint Venture
Starbucks	Tata Global Beverages	USA	Consumer	Joint Venture
Marriott International Inc	Prestige Group	USA	Hospitality	Joint Venture
Macquarie	State Bank of India	Australia	Financials	Joint Venture
QBE	Prism Johnson	Australia	Financials	Joint Venture
Walmart	Flipkart	USA	E-commerce	M&A
Vodafone	Idea Vodafone	UK	Telecom	M&A
ING	Vysya Bank	Netherlands	Financials	M&A
Coca Cola	Parle Bisleri	USA	Consumer	M&A

Historically, a joint venture (JV) followed by an IPO where the MNC retains a majority stake upon listing has been the most common model. A similar model, but where the MNC is a minority shareholder upon listing, often occurs due to sector-specific regulatory requirements (for example, insurance). Franchise and distribution agreements are common but have been met with mixed success. Jubilant Foodworks has been successful in rolling out Domino's Pizza, for example, while Westlife has been largely unsuccessful with McDonald's.

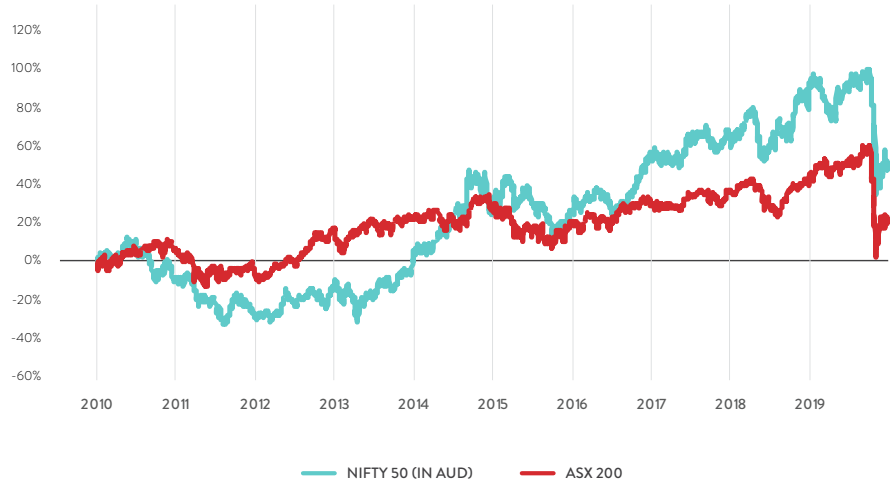
In more recent years, global leaders in the technology sector have chosen to enter India via mergers and acquisitions (M&A) and venture capital (VC) like investments. China's two technology giants, Alibaba and Tencent, have been the most aggressive in terms of investing in Indian startups and unicorns. It is estimated that more than half of India's 30 unicorns have received investment funding from either Alibaba or Tencent. Meanwhile, Walmart's acquisition of Flipkart (e-commerce) for US$16 billion provides a good example of M&A being used as a quick and efficient Indian market entry strategy.

The remainder of this section analyses different case studies of MNCs with operations in India. However, before delving into the specifics, it is important to highlight why Australian companies should look to invest in India. First of all, the size of the market and the spending power of India's rising middle class is incredibly powerful, especially for companies with a small home market like Australia. Secondly, India is one of the best structural growth stories in the world, with growth driven by demographics, infrastructure build and technological leapfrogging. This is a sharp contrast to many developed markets which are increasingly dependent on ultra-loose monetary and fiscal policies to generate growth that ends up being primarily cyclical.

Thirdly, India offers diversification for Australian corporates. India is largely a domestic demand economy and it is a major importer of commodities, particularly oil. As such, the business cycle in India can often be uncorrelated to commodity-exporting countries like Australia. The consumer side of the Indian economy is also significantly influenced by monsoons. The monsoon season in India accounts for approximately 70 per cent of annual rainfall. Indian weather patterns are uncorrelated with drivers of consumption in other parts of the world, which provides diversification benefits for consumer facing MNCs.

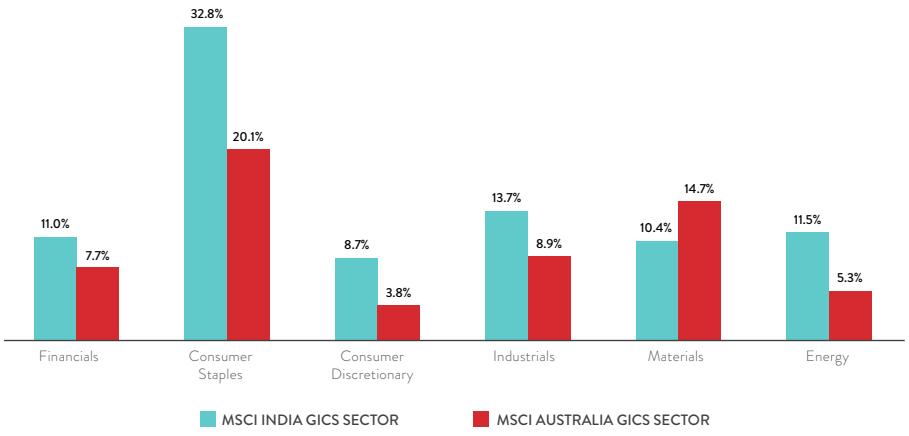
And finally, India is a high-return market. As shown below, return on equity (ROE) in all major sectors (except materials) is higher in the India market than in Australia. This translates into returns for shareholders, with stock price returns of the NIFTY 50 (in AUD) outperforming the ASX 200 significantly over the last decade.

FIGURE 19. *10-year NIFTY 50 price performance versus ASX 200*



Source: Bloomberg as of May 17, 2020.

FIGURE 20. *Return on equity last FY in key sectors: India versus Australia*



Source: Bloomberg as of May 17, 2020. ROEs are calculated using MSCI GICS Sector data for the last financial year

The case study discussion consists of three main parts. The first section, *What has worked*, provides case studies of foreign companies operating in India that have successfully developed business models to drive market share, profitability and outstanding returns for shareholders. These examples include ICICI Prudential Life Insurance, Hindustan Unilever, Nestlé, Maruti Suzuki, Abbott Labs and Macquarie Group. The second section, *What can go wrong*, outlines examples of foreign companies that have failed to thrive in India, namely Apple, Kellogg's and General Motors.

The final section, *Why now*, highlights that there is a scramble going on for new economy assets in India and also touches on recent incentives offered by the Indian government for MNCs to relocate manufacturing facilities out of China into India.

Engaging with India: What has worked

ICICI Prudential Life Insurance

ICICI Prudential Life Insurance is a joint venture (JV) between ICICI Bank, one of India's largest private sector banks, and Prudential Life Insurance Plc of the UK. The company began its operations in fiscal year 2001 and currently has more than 750,000 life insurance policies and generates total annual revenues of approximately $7 billion. The company also has assets under management (AUM) of approximately $30 billion, making it one of India's largest fund managers, in addition to being one of the largest insurers. The firm was the first Indian life insurer to IPO in 2016 and the company currently has a market cap of $12 billion[40].

There are a number of reasons why this JV has been so successful. Firstly, life insurance in India is a massively underpenetrated sector. Prudential recognised this opportunity for growth more than 20 years ago, but the regulatory environment at the time was not conducive to foreign investment. There were no publicly traded life insurance firms and a maximum allowable stake in a private life insurance company was limited to 24 per cent for a foreign entity. ICICI and Prudential therefore drafted a shareholder agreement which granted Prudential 24 per cent ownership but also gave them the right of first refusal on another 25 per cent once foreign ownership regulations were liberalised.

A second factor in the success of ICICI Prudential Life is the company's core philosophy of customer centricity. Products were designed specifically for Indian customers with differences in lifestyle, longevity, income levels and geography in mind, and products were priced very competitively for the Indian market. While putting the customer first seems obvious for any business anywhere in the world, as outlined in the next section, truly understanding the Indian customer is one aspect of engaging with India that many MNCs get wrong.

Thirdly, ICICI Prudential successfully combined the strengths of each company while empowering local management. ICICI Prudential's founding members, like current CFO Satyan Jambunathan, speak very highly of the systems, processes and product knowhow that Prudential brought into the JV and how these complemented ICICI's distribution strengths, call centres, customer service and fulfilment capabilities.

Hindustan Unilever

Hindustan Unilever (HUL) has a long and enviable history of operating in India. Nascent operations can be traced back as far as 1888. Lever Brothers in India was established in 1933 and listed on the Bombay Stock Exchange in 1956. Unilever continues to own a majority stake in Hindustan Unilever, which is now the largest FMCG company in India. It has a market cap of over $100 billion, annual sales of approximately $8 billion, 35 product brands in 20 different categories and more than 18,000 employees. However, it is not just the company's size that is impressive – it is its profitability. With return on equity of approximately 83 per cent, it is one of the most profitable FMCG companies in the world.

Hindustan Unilever focuses on the following "winning" strategies: Winning with Brands and Innovation, Winning in the Marketplace, Winning through Continuous Improvement and Winning with People. While these have all been instrumental in HUL's success, it is its Winning in Many Indias (WiMi) program that stands out as a key success factor and holds the most lessons for other MNCs.

The WiMi strategy divides India into 15 clusters and appoints business heads for each cluster to address the fact that India is not a homogeneous country, but one with multiple languages, cultures, spending behaviours, tastes, preferences and product requirements.

A related aspect of WiMi is the company's distribution strategy, which is tailored to the complex nature of distribution in India. More than 80 per cent of sales occur through neighbourhood 'mom and pop' stores and out of a total of 11 million retail touch points in India, HUL reaches over eight million. The combination of the right products distributed the right way has made Hindustan Unilever an unstoppable force in the Indian consumer sector.

Nestlé India

After India's independence in 1947, the Indian government implemented policies that focused on local production of key goods, including dairy. Nestlé responded to India's aspirations, entered the Indian market in 1956 and set up its first major production facility at Moga in Punjab in 1961. From these humble beginnings, Nestlé has grown into one of India's largest FMCG companies. It listed in 1991 at a price of INR 63 and today the stock price is over INR 16,000. The company has a market cap of $32 billion and Nestlé's parent continues to own approximately 63 per cent.

The fact that Nestlé's entry into India was responding to a government directive is an important point for MNCs looking to engage with India in the current environment. As discussed later in this section, the Indian government is again enticing foreign investment into India as it sees the current US-Sino tensions as an opportunity for global reorganisation of supply chains.

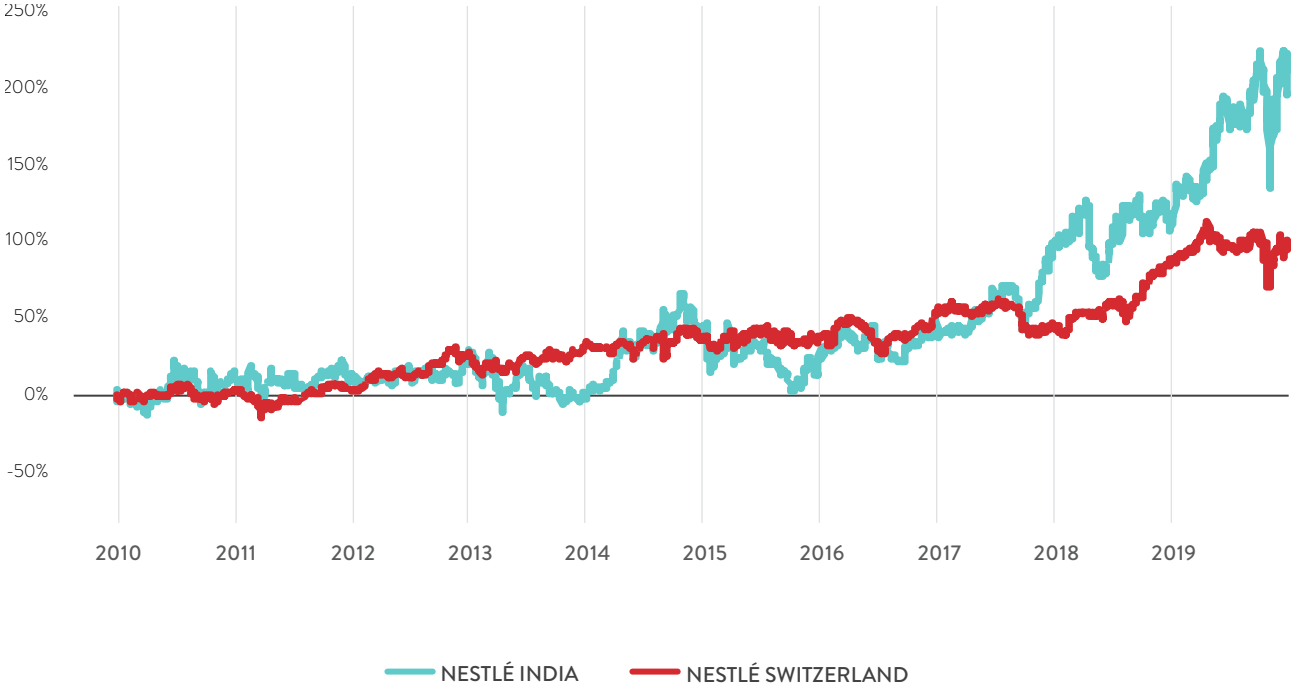
Nestlé also adopted a localised approach to both product development and marketing. Nestlé's Maggi brand of instant noodles was launched with local flavours (Maggi Masala noodles, for example) which align with local tastes and preferences. Like Hindustan Unilever, Nestlé's marketing strategy focused on a 'many Indias within India' approach.

An additional area where Nestlé has excelled is Know Your Customer (KYC) product development. For example, in the early years, Nestlé's two-minute noodles campaign for Maggi focused on liberating the Indian housewife from the daily cooking ritual.

This helped increase penetration for Maggi as an efficient and healthy snack option for Indian households. More recently, Nestlé has repositioned a number of its brands from convenience snacks to health and nutrition and has launched organic variants for a number of its product categories.

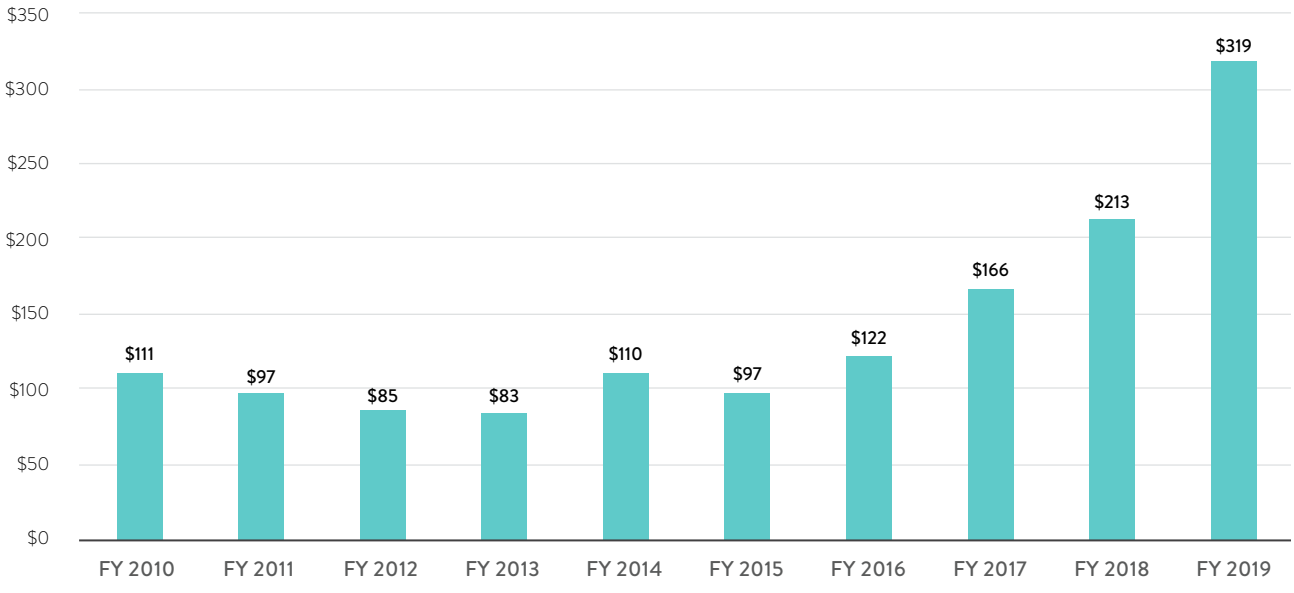
These tactics have certainly paid off. In the last 20 years, Nestlé India's stock price has outperformed the parent stock price by approximately 100 per cent. In addition, Nestlé India has distributed more than $1.4 billion of total dividends in the last 10 years, with an average payout of over 60 per cent. This has been very beneficial to the parent company, which remains the majority shareholder.

FIGURE 21. *Nestlé & Nestlé India 10-year stock price performance*



Source: Bloomberg

FIGURE 22. *Nestlé annual dividends 10-year performance (AUD millions)*



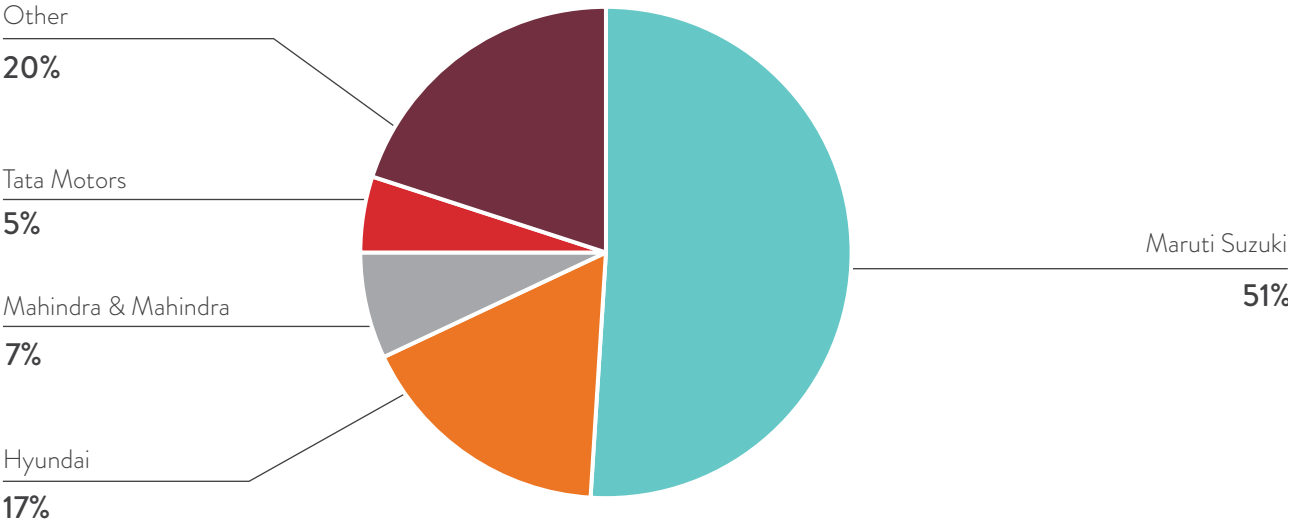
Source: Bloomberg

Maruti Suzuki

Maruti Udyog Limited (MUL) was founded by the Indian government in 1981 and was merged with Suzuki Motor of Japan in 1982, after the latter won a bid to collaborate with MUL. By the time the Indian auto market was liberalised in 1992, Maruti Suzuki (MSIL) was already well established with unrivalled economies of scale and cost efficiencies. To protect its first mover advantage, Suzuki invested heavily in component manufacturers and sent Maruti employees to Japan for extensive training. Suzuki's holistic approach of foreign direct investment (FDI) (car manufacturing, auto parts, dealership network, transfer of technological and management knowhow) has continued to set Maruti Suzuki apart from other foreign auto majors.

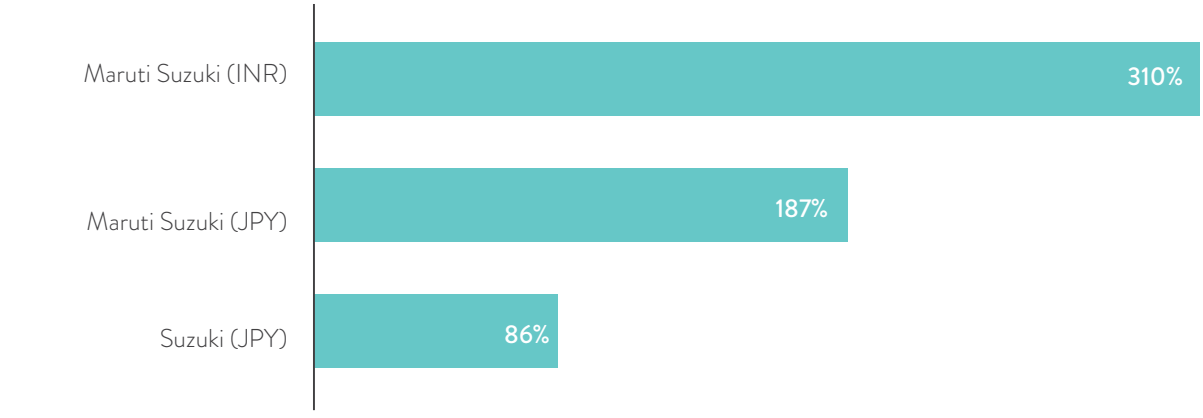
Maruti Suzuki now has a market cap of $32 billion, larger than Suzuki's market cap of $20 billion. As shown below, the company has approximately 50 per cent market share in passenger vehicles while other MNCs, excluding Hyundai, have hardly gained any traction over the past two decades. The seed that was planted in the early 1980s, while initially nurtured by government protectionism, has nevertheless grown into a very profitable asset and a trusted brand.

FIGURE 23. ***Indian passenger vehicle market share FY20***



Source: SIAM, CLSA for market share. Bloomberg for stock price performance.

FIGURE 24. ***MSIL vs Suzuki stock price performance since 2000***



Source: SIAM, CLSA for market share. Bloomberg for stock price performance.

Abbott Laboratories India

Established in 1910, Abbott India is one of the country's oldest and most trusted healthcare companies with more than 400 pharmaceutical brands, nutritional products, medical devices and diagnostics solutions. Abbott India is a 75 per cent owned subsidiary of US pharma company Abbott Labs.

The Indian pharma market presents a number of challenges for foreign companies including intellectual property rights, price controls, US Food and Drug Administration (FDA) uncertainties and an underdeveloped primary health care system. In addition, India is also home to several large and successful domestic pharma companies including Sun Pharma, Dr Reddy's, Lupin and Cadila. How did an American company grow to become a major player in a country with a complicated operating environment dominated by home-grown pharma giants?

Firstly, Abbott was early to get in on the ground and has now been present in India for over 100 years. It then used strategic M&A to bolster this early foothold. The acquisition of the formulations business of Piramal Healthcare for $3.7 billion in 2010 is a good example of this strategy.

Secondly, like ICICI Prudential, Abbott has a customer-centric model and its stated mission is "to enhance the health and well-being of Indians". To achieve this, the company focuses on local research and development (R&D) for localised solutions and has more than 130 Abbott scientists who conduct R&D to meet specific Indian needs.

Thirdly, Abbott India holds an important position in Abbott's global operations and has the attention of and buy-in from Abbott's top management team. Abbott's Global CEO, Miles While, has been in the top position for over 20 years and is a strong supporter of the Indian business. He says: "India is an investment priority. India is fundamentally important to Abbott. We are proud of the work we do in India and we believe it makes a substantial positive impact to the health of Indians."[41]

Macquarie Group

While the examples above are primarily from the US, Europe and Japan, it is important to highlight that there are also Australian companies that have successfully entered and thrived in the Indian market. In 2005 Macquarie Group established a securities brokerage business. Importantly, the entry into India came shortly after Macquarie's purchase of ING's Asian Equities business in 2004. This transaction gave Macquarie access to Asian equities in 10 locations (Hong Kong, the Republic of Korea, Japan, Taiwan, Thailand, Singapore, China, Indonesia, Malaysia and the Philippines), but not in India. The decision to launch organically in India was thus a strong complement to the firm's broader strategic engagement with Asia as a region. This played an important role in driving Macquarie's early success in the Indian market.

In 2009 Macquarie forayed into the infrastructure space by partnering with the State Bank of India (SBI) to launch the Macquarie SBI India Infrastructure Fund. Like other examples of MNC success in India, SBI and Macquarie brought a unique combination of local and international expertise to the joint venture. SBI is the largest project finance arranger in Asia and the largest lender in India with a deep knowledge of the country's infrastructure sector, while Macquarie's well-known financing abilities helped raise approximately $1 billion in an exceptionally challenging post-GFC market.

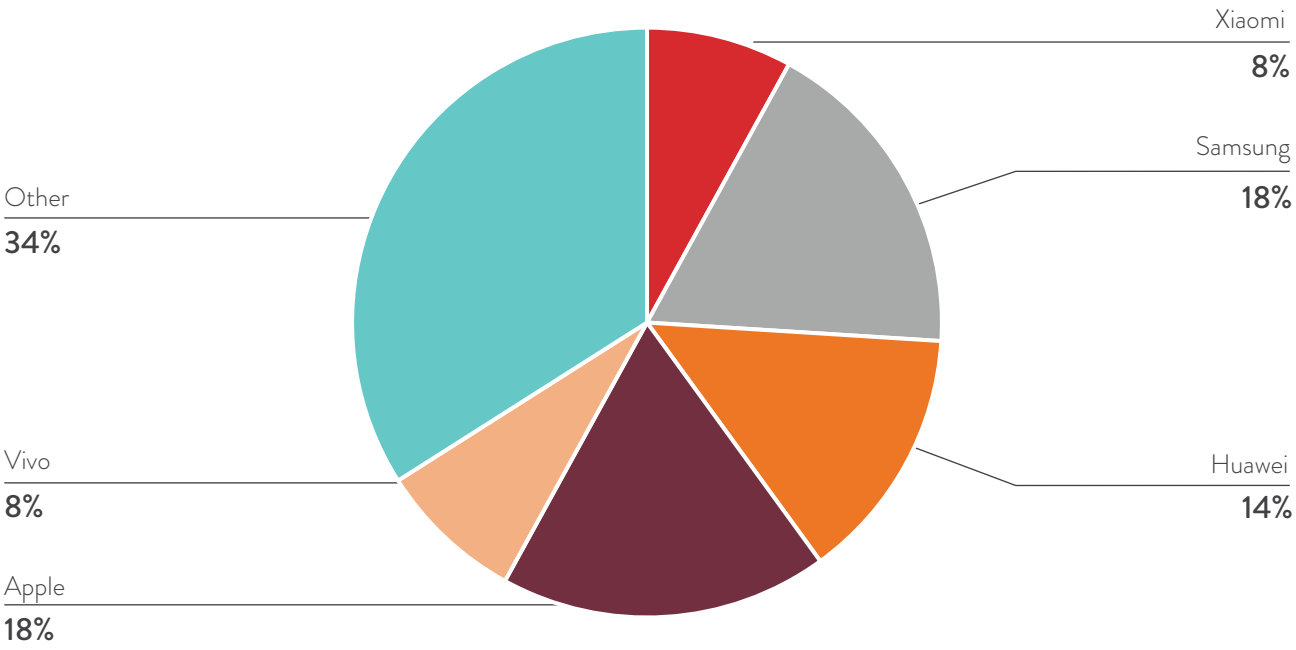
Macquarie Infrastructure and Real Assets (MIRA) entered the Indian market in 2013. In 2018 MIRA won the bid for nine road assets covering more than 600 km of national highways under a Toll-Operate-Transfer (TOT) model. This was one of the largest inflows of FDI into the sector at the time and Macquarie is the largest foreign investor in Indian roads.

Engaging with India: What can go wrong

Apple

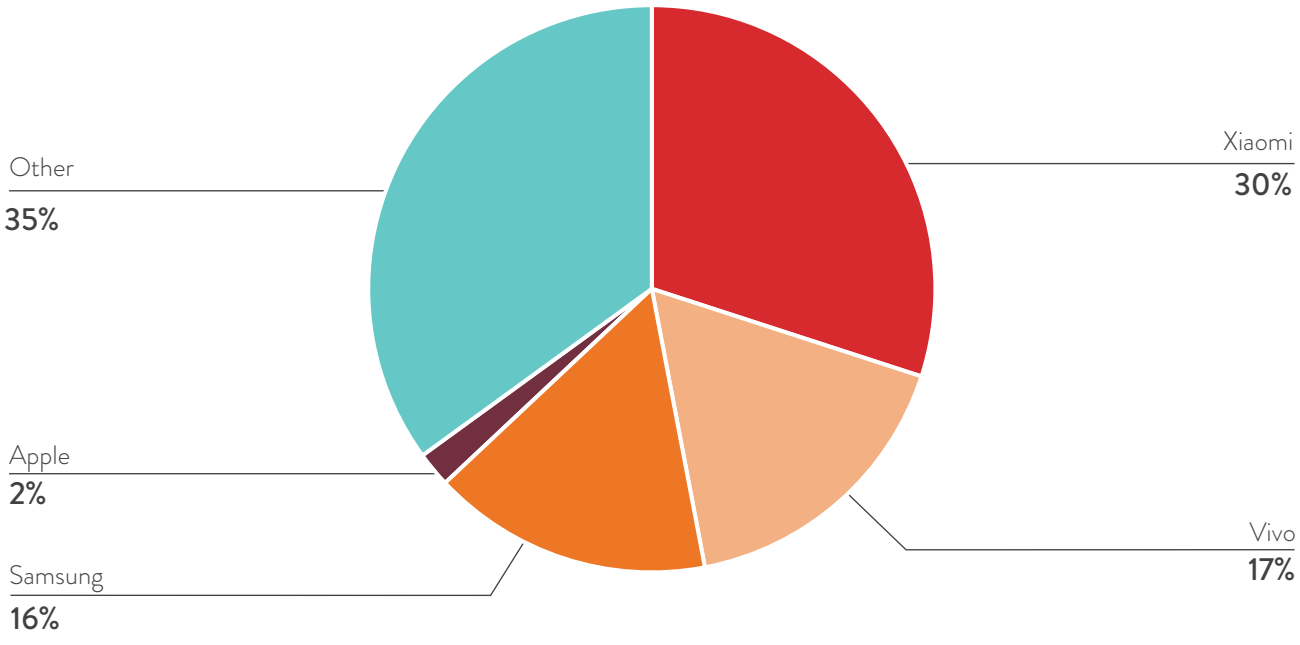
Apple is one of the world's largest and most profitable companies, yet it only has about two per cent market share in India. By contrast, Chinese smartphone companies Xiaomi and Vivo have 30 per cent and 17 per cent of market share in the Indian smartphone market, followed by South Korea's Samsung with 16 per cent. Given the size, growth and demographic profile of India (young, connected, tech-savvy), how did things go so wrong for Apple? There are a number of theories as to why Apple appears to have failed in the world's second-largest consumer market.

FIGURE 25. ***Apple's smartphone market share globally***



Source: Counterpoint Research. Market share data for global is as of 4Q19. Data for India market share is as of 1Q2020.

FIGURE 26. ***Apple's smartphone market share in India***



Source: Counterpoint Research. Market share data for global is as of 4Q19. Data for India market share is as of 1Q2020.

Firstly, Apple did not appropriately alter its product nor, more importantly, its price point to suit Indian consumers. According to IDC, the average selling price of smartphones in India is approximately US$160, yet the cheapest iPhone sold in India (the SE) costs approximately US$550.

Secondly, Apple does not have the same physical, on the ground presence as its competitors. Samsung had first mover advantage in India after entering the market in 1995 in a JV with a local partner for TVs. Samsung, Xiaomi, Oppo and Vivo all have local smartphone assembling factories in India. Apple does too, but it's done through third parties such as Foxconn and Wistron so there is no brand recognition or feet on the ground. In terms of physical retail presence, Samsung has approximately 2,000 stores, Xiaomi has 1,000 'Mi stores' and Vivo has 350 stores across India. Apple, meanwhile, is not expected to open its first retail store in India until 2021. All of Apple's offline sales are done through official resellers.

Finally, Apple has not been successful in securing local tie-ups. Xiaomi, for example, has an exclusive agreement with Flipkart to be the official reseller. Samsung has a strategic alliance with Bharti Airtel for exclusive models. Oppo and Vivo, meanwhile, have gone down the marketing route and are major sponsors of Indian cricket teams. Apple has been left out in the cold. Winning market share in the Indian market now will be very difficult and expensive for Apple.

Kellogg's

Kellogg's entered India in 1994 with the aim of selling its breakfast cereal and other snack foods to the large, growing Indian middle class. Not surprisingly, Corn Flakes was used as the star market entry product and Kellogg's decided to invest approximately $65 million in the launch. Unfortunately, Kellogg's significantly mismanaged the cultural aspects of product promotion and implemented a campaign that suggested that traditional Indian breakfasts were not nutritious.

Corn Flakes were largely unsuitable for the Indian palate and Kellogg's failed to recognise that many Indians are used to consuming milk hot and sweetened, rather than poured cold on relatively flavourless cereal. Without adequate research on appropriate price points and despite the lacklustre response to Corn Flakes, Kellogg's continued to roll out other products including Wheat Flakes, Frosties, All Bran, Special K and Coco Chocolate Puffs, none of which were met with the success they had achieved in developed markets. Kellogg's then tried to "Indianise" the product offering by developing coconut and elaichi variants of Corn Flakes, but these were also met with a lukewarm response.

Today Kellogg's has significant market share in the local cereal market, so to say it is a complete failure would be unfair. However, after more than 25 years after market entry, India still contributes less than 15 per cent of Asia-Pacific revenues and less than three per cent of total global revenues. In addition, Kellogg's is now in the unenviable position of having to vigorously defend market share in a category it created. Local brands like Bagrry's, Britannia and Saffola (Marcio) offer similar but less expensive products and other MNCs like Nestlé and Quaker (PepsiCo) have created a highly competitive and crowded market for breakfast foods.

General Motors

General Motors (GM) entered India in 1928 and tried a number of different business models, all of which failed to make meaningful inroads in the Indian passenger vehicle market. Most recently, in 2015, GM developed a US$5 billion investment plan along with SAIC Motor of China to manufacture around two million vehicles a year and sell them to other emerging markets in Asia and Latin America. GM set a target of increasing its market share in India to three per cent by 2020. Instead, its market share fell below one per cent and in 2016, after more than 20 years of operation in India, GM announced plans to no longer sell cars there as of 2017.

What went wrong? Like Apple, the post-mortem on GM in India suggests that it did not sufficiently localise the price point or the product to suit the Indian market. The fact that Indian factories were used to supply numerous emerging markets highlights the lack of attention to localisation. Secondly, it chose the wrong partner in SAIC Motor. SAIC is a state-owned Chinese company headquartered in Shanghai and therefore could not bring local knowledge to the design, manufacturing or distribution process.

Engaging with India: Why now

There are two reasons creating a sense of urgency for Australian companies to engage more meaningfully with India: (1) the scramble for new economy assets in India is driving up valuations and may crowd out companies that are late movers; and (2) the Indian government is currently offering incentives to induce FDI out of China and into India, which will benefit all foreign companies wishing to engage.

The scramble for 'new economy' India

In 2018 Walmart announced that it had paid US$16 billion for a majority stake (77 per cent) in Indian e-commerce giant Flipkart. This was a very calculated move intended to head off Amazon in India. Interestingly, Chinese internet juggernaut Tencent was already a minority shareholder in Flipkart so both US and Chinese mega-cap companies are now in a land grab for prime assets in Indian e-commerce.

A similar situation has occurred with the largest payments company in India, PayTM, which at the last round of private equity financing was valued at approximately US$16 billion. Japan's SoftBank, which first invested in the company in 2017, holds a 19 per cent stake and Alibaba, both through Ant Financial and via Alibaba directly, is the largest shareholder with 38 per cent.

Finally, consider the scramble for Reliance Industries assets. Reliance is India's largest company with a market cap of over $200 billion. In August 2019, Reliance announced that Saudi Aramco, the world's largest oil company, was buying a 20 per cent stake in its energy, refining and petrochemical assets for US$15 billion. Then, in April 2020, Facebook announced that it was taking a 10 per cent stake in Reliance's digital assets (Jio Platform) for US$5.7 billion. Facebook has approximately 346 million users in India and WhatsApp has over 400 million, making India the biggest market for Facebook globally.

These are examples of big foreign companies investing in big Indian companies and this trend is setting the state for further large-scale FDI. Companies that delay engaging with India may find themselves priced out of the market and far behind other MNCs.

Current incentives to invest in India

The Indian government is currently actively courting FDI. According to press reports, in April it contacted more than 1,000 companies in the US and other markets to offer incentives for manufacturers to relocate out of China[42]. Prime Minister Modi has told states to be ready with pro-investment policies to attract FDI with medical equipment, food processing, textiles and auto parts earmarked as priority sectors. India's cabinet has also announced a production-linked incentive (PLI) scheme for the electronics sector and announced a major corporate tax cut in 2019.

The rationale for these moves is obvious. India has taken the view that the tensions between the US and China, which started in 2018 with the trade war and have been exacerbated by COVID-19, present a one-time opportunity for reorganisation of global supply chains and they don't want India to miss out. To date, countries like Vietnam and to a lesser extent Cambodia, have received the majority of supply chain reorganisation investment, but India is determined to change this trend.

Conclusion

The case studies presented above show that India provides MNCs with access to structural growth, enhanced profitability, diversification and dividends, all of which can add up to superior shareholder returns if executed properly. Every year that Australian companies delay engaging with India is another year when global competitors can potentially grab an opportunity, secure a local partner, gain an edge in terms of local knowledge or win market share that is difficult and expensive to win back. So start investing in India now. India is too big to ignore.

PART B: AUSTRALIAN MULTINATIONALS DOING BUSINESS IN ASIA – CASE STUDIES OF EIGHT AUSTRALIAN PUBLIC AND PRIVATE COMPANIES

By Mukund Narayanamurti, Chief Executive Officer, Asialink Business

Public company case studies

CASE STUDY

COCHLEAR: BASED ON AN INTERVIEW WITH DIG HOWITT, CHIEF EXECUTIVE OFFICER & PRESIDENT

Cochlear, the Australian company formed to commercialise the invention of the cochlear hearing implant four decades ago, will open its first factory outside of Australia in Chengdu, the capital of China's Sichuan province, in late 2020.

Cochlear's mission is to build on its global leadership in innovation of hearing implants, as well as its market leadership in production and clinical services. It recognises that to retain global leadership over the long term, it needs to lead in China.

MAKE IN CHINA, LEAD GLOBALLY

Developed country markets for hearing implants and many other medical devices continue to provide significant growth opportunities and are Cochlear's biggest driver of growth. Emerging markets are also an important driver of Cochlear's growth, none more so than China. Cochlear CEO Dig Howitt explains: "There's a big market here. You've got a government saying they want China to be a manufacturer of medical devices. When you put those two things together you can see there are going to be successful cochlear manufacturers in China over the next 20 years. We want to be one of those." When Cochlear decided to expand its manufacturing capacity, the decision to build a factory in China logically progressed.

The market opportunity in China is vast, but trends do not favour imports. "If you look at where medical devices are in China now and look back over the last 20 years, you can see that locally produced devices, made by local companies or multinationals with a local presence, dominate nearly all segments. Stents are a good example of this. Cochlear implants and pacemakers which are still largely imported are exceptions," says Howitt. Cochlear expects to evade this trend by becoming a domestic manufacturer.

Cochlear seeks to lead in all market segments in China, and recognises the need to adapt for price sensitivity. While there can be no compromise on quality, Cochlear looks closely at the needs of the local market and has already succeeded in shifting some consultations online. Howitt uses an aviation analogy: "Jetstar doesn't aim for a lower safety record than Qantas. We aim for the same reliability of our implants whatever the segment they are sold in. Some of the service and features around that will be different." Cochlear believes that establishing a manufacturing presence in China will help it better support the specific needs of its Chinese customers.

THINK IN DECADES

Cochlear's commitment to manufacturing in China aligns with China's long-term manufacturing strategy, Made in China 2025, which encourages global market leaders in advanced manufacturing to set up in China. Hearing is also an essential part of the health policy plank of China's 2049 strategy to reach full developed country status. This means where it can Cochlear can align its expansion plans with the strategies of policymakers who also think in decades. Says Howitt: "Our interests are aligned in that we want children to hear." This is particularly important in a country where the government sets competition policy and is also the single largest buyer of hearing implants for children.

Cochlear has also closely aligned with provincial policy goals by supporting Chengdu's plan to become a major centre of innovation in medical devices. It has established a joint venture with the Sichuan Innovation and Entrepreneur Promotion Agency (SIEPA), a government authority that brings together private and public investment to attract high-tech businesses. SIEPA and Cochlear are working together to create the Chengdu Hearing Hub at the Tianfu Science City in Chengdu. Cochlear brings expertise gained from being a key member of the Australian Hearing Hub on Macquarie University's Sydney campus.

CASE STUDY

CARSALES: BASED ON AN INTERVIEW WITH PAUL BARLOW, MANAGING DIRECTOR INTERNATIONAL

Carsales' unique lead generation-based business model has enabled its leadership of online vehicle sales since its establishment in 1997.

A sharply honed understanding of its global competitive advantage has driven its international expansion into four Latin American markets and South Korea over the past decade.

ONLINE EXPERTS, NOT ADVERTISERS

Paul Barlow, Carsales Managing Director International, explains that Carsales positions itself as experts in online sales rather than as advertisers. "If you look around the world at all of our peers, the most common business model is a subscription-based model, where car dealers are the number one clients of online automotive verticals and they usually pay a monthly fee to advertise. Carsales differs from that. We have a pay per lead model." The more leads Carsales provides, the more it helps dealers sell cars. Barlow adds: "We are very aligned with educating dealers on the best way to handle these leads. We help them convert from a lead to a sale."

In internationalising its business, Carsales has sought to acquire leading online car sales businesses that can benefit from its expertise. Barlow explains that in new markets they "look for a business that is a number one or a number two that can challenge to be number one. We find a business where our technology or our IP can accelerate the growth of that business. And then we look at whether we work with a partner."

In its Mexico, Argentina and Chile acquisitions, Carsales took controlling stakes. But in its first deal with Webmotors in Brazil and its most recent and largest deal with SK Encar in South Korea, it began with establishing strategic partnerships by purchasing minority stakes. Both deals involved long negotiations.

Carsales emerged from four years of negotiations with Webmotors' owners Banco Santander as more than just a strategic partner in Brazil's largest online vehicle sales business. It had also gained a sharply defined understanding of its global competitive advantage. Carsales took this experience into its largest deal yet. The purchase of a minority stake in Encar, South Korea's largest online used car sales platform, from SK Group, one of South Korea's giant 'chaebol' conglomerates, also took four years. In 2018 Carsales took its stake to 100 per cent.

Barlow explains: "In South Korea what we brought to Encar was a different way of thinking. We come from a dealer servicing background. Most of our peers from around the world come from advertising or in the SK Group example, big conglomerates, one of the chaebols. Encar was an offline and an online business. They saw that we are online specialists."

Barlow goes on to explain the particular value its back-end expertise offered to Encar. "In the back end we're integrating the dealer into all different systems, whether it's inventory management, pricing, or CRM etc. Then it's about partnering with the dealers and monetising from there."

APPEARANCES CAN BE DECEIVING

For global businesses seeking to expand into South Korea, the chaebols' dominance of the economy can make it difficult to read opportunities. This is particularly the case in online sales, as South Korea is one of a handful of countries where local search engines are much more popular than Google. Through its acquisition of Encar, Carsales now dominates online used car sales in South Korea, a market segment that used to be the domain of one of the largest chaebols. Carsales understood that while the South Korean government supports the dominance of chaebols in the economy, it will occasionally intervene in the interests of consumer protection. When legislation obliged SK Group to divest from Encar, Carsales' understanding of the market and its unique offering positioned it to make a decisive offer.

CASE STUDY

IDP EDUCATION: BASED ON AN INTERVIEW WITH ANDREW BARKLA, CHIEF EXECUTIVE OFFICER

In the early 1960s, a conversation between Indonesia's Minister for Higher Education and Australia's Ambassador in Jakarta posed the question: "Is there a role for Australia to share agriculture science learnings with Indonesia?"

This discussion planted the seed for the start of IDP, an organisation that, in time, would grow to be a world leader in its sector. IDP would go on to help nearly half a million people achieve an international education through its global office network, and co-own the world-leading English language test, IELTS.

Over the past five years, IDP has continued to invest in its physical network, but has undergone a digital transformation that has dramatically expanded its service offering. When CEO Andrew Barkla took IDP Education public in 2015, he did so with the mission to build the world's leading platform to support students through the entire course of their international education journey. Under Barkla's leadership, IDP Education has integrated its physical network with a new online platform. This has enabled it to become the global leader in student course searches, streamline its existing student placement and English-testing services, and further extend its offerings in student events, in-country support and careers advice and placement.

DIGITISE TO GROW

Over decades, IDP Education extended its core offering to focus on English language testing, student placement services and English language teaching.

Barkla recognised IDP Education's established physical network of offices around the world placed it ahead of any competition as a provider of these services to students seeking to study in Australia and other leading study destinations. He also saw that as students increasingly looked to online services to plan their overseas study, IDP Education needed to step up its engagement in the digital space.

Barkla describes the strategy IDP Education adopted as "first and foremost focused on leveraging digital capabilities to connect closer with students, enabling us to go well beyond what you can reach as a physical organisation".

He explains: "I saw that if we didn't move past organic growth, we risked insurgents disaggregating the market. Our goal was not to turn our back on organic growth, but to change the DNA of the company by building in digital capability that focused on customers.

"The digital business enables us to accelerate new services based on data and insights and engagement that universities and potentially other parties can take advantage of."

IDP Education's acquisition of international course search company Hotcourses in 2017 accelerated the company's digitisation. Barkla says: "When we acquired Hotcourses it was the most engaged digital platform for international student searches on the planet. The site registered 65 to 70 million searches, with universities around the world using it to represent their courses. We took this in alongside our own new digital footprint, and brought in some deep technologies around marketing, automation and lead scoring, as well as new people."

SCALE TO INNOVATE

Through its hybrid strategy, IDP Education has evolved from an international company focused on supporting students coming to Australia to a global company connecting students to universities all over the world. To drive innovation, a new digital campus was built in Chennai that brought together more than 400 digital experts. Adding to this new capability, 16 new strategic roles in every region, particularly in digital marketing, has given the company the capacity to manage and grow a much larger pipeline.

Barkla explains the possibilities greater scale creates for the company. "If you take the organic strategy, it was about taking the many countries we were in sourcing students to primarily service Australian clients, and through the last decade building capability in those countries to serve university clients in the US, Canada, the UK, New Zealand and Ireland."

At the same time the company has gained the capacity to engage digitally with students through the early stages of search, which creates data on student preferences and propensities. "I would say we have built the largest student dataset in the world. What you can do with that is only limited by your imagination."

Integration of its physical networks and digital platform has helped IDP Education maintain its global leadership in the provision of services to international students. It has also positioned the company as the leading innovator of its industry. The services IDP Education is developing for university clients using its new datasets is a strong example of this leadership. Barkla explains: "We're using the data to accelerate the growth of our business. We are building a marketplace at the moment where universities can come to us and define what kind of student cohort they want, specifying the kind of diversity or student credentials they are seeking. This will change the whole model of the industry. In that context we will leave behind the vast majority of our competitors."

CASE STUDY

LENDLEASE: BASED ON AN INTERVIEW WITH TONY LOMBARDO, CHIEF EXECUTIVE OFFICER - ASIA

For generations, Lendlease has been Australia's global construction company. Since a strategic review in 2007, it has built its business around six key trends it sees shaping global property development over the coming decades – urbanisation, infrastructure, ageing populations, funds management, technology and sustainability.

Lendlease identified 17 'gateway cities' around the world where these trends and the company's competitive advantages intersect.

In Asia, Lendlease's gateway cities are Beijing, Shanghai, Tokyo, Kuala Lumpur and Singapore. Focusing on these cities has helped Lendlease build on its long-established reputation as a global provider of construction services to establish itself as a leading property developer and funder of property development projects.

BUILD CONFIDENCE WITH EACH PROJECT

Lendlease Asia CEO Tony Lombardo describes how successively more ambitious property development projects have helped Lendlease entrench itself as a local player in Singapore. Lendlease commenced its first Singaporean development as an investor in the 313@ somerset shopping centre in 2007. Lombardo explains the success of the project showed that "we knew we could develop; we knew we could invest capital. It gave us the confidence to start moving the business forward."

Lendlease's next investment, Jem, which started its operations in 2013, is a mixed office and retail development that supported the Singapore government's Jurong East urban renewal project. Lombardo says: "Every time we do a big project people can see how Lendlease really operates. That gives our investors confidence that we do have something different to offer, and I think they are able to appreciate that we are able to export our urbanisation strategy to the rest of the world." Lendlease took its next step in Singapore in 2015 when it secured the Paya Lebar Quarter urban renewal project, which integrates residential, office and retail space.

Lombardo credits its growth in Singapore to setting a long-term strategy and committing to the market.

"For Australian companies, my big thesis is make sure your strategy's right, make sure you understand what you're trying to deliver," he says. Beyond having a clear understanding of competitive advantage, Lombardo stresses this means you need to "make sure you're making portfolio moves that will allow you to step up once you get confidence to grow your business. It's an evolution, it can't be a short-term decision."

MATCH TRENDS TO YOUR STRENGTHS

Lendlease has an independent research team constantly reviewing global trends. When exploring new opportunities, Lombardo says: "We as a management team on the ground then look at it from our microanalysis and determine whether or not we can operate and take advantage of some of the things we're looking at from a macro level."

Lendlease's macroanalysis supported the decision to pursue an aged care residential complex in Qingpu, just outside Shanghai. Demographic trends in this part of China show a rapidly ageing population – Shanghai alone is expected to have six million people older than 60 by 2021. Chinese government policy encourages the expansion of the aged care sector, including the development of residential care, and encourages foreign investment. This creates incentives for government officials at all levels to collaborate with companies with demonstrated capacity.

Lendlease's decision to enter residential aged care in China was also supported by the company's microanalysis of conditions in the market and its own capacity to deliver. From an operational perspective, Lendlease draws on more than two decades of experience delivering construction services in China. Since Lendlease is also recognised in China as the leader in senior living and aged care, the company was well-positioned to attain local government approval.

The first phase of the project, the $400 million construction of 850 low-rise apartments, commenced in 2019. Lendlease sees it as a pilot and anticipates much greater investment in China's aged care sector to follow.

INVEST IN PEOPLE

Lombardo stresses how important attracting the right employees in each market has been to Lendlease's success in Asia. "We are continuing to attract more and more of that talent. Once upon a time that was hard to do," he says. Lendlease's expansion into property development and funding across multiple Asian markets has sent strong signals that the company is a committed player, which makes recruitment easier. Lombardo explains that Lendlease in Asia has been proactive in building local management and reducing the need for expatriate appointments. In 2018, Lendlease in Asia began a program that sends local employees on secondments to other regions of the world. "We're trying to give our people in Asia the right levels of skills, so they know how Lendlease works. We've become an exporter of Asian talent abroad with a view that key talent is going to return to run our platform."

CASE STUDY

XERO: BASED ON AN INTERVIEW WITH KIRSTY GODFREY-BILLY, CHIEF FINANCIAL OFFICER AND KEVIN FITZGERALD, MANAGING DIRECTOR - ASIA

For over a decade, Xero's cloud accounting software has been helping small and medium sized enterprises (SMEs) simplify their business back office functions.

Xero's applications allow businesses to better track inventory, payroll, billing and many other business functions in real time. Its tax and reporting functions help businesses meet their obligations and measure their performance. Since it is a cloud computing platform, businesses can access their ledger from any location using any operating system. In addition, Xero has an open API, meaning that developers can work with Xero to design plug-ins that create extra functionality. There are more than 70,000 users of Xero's API developer tools and over 800 connected apps in Xero's ecosystem. In Australia and New Zealand, over a million businesses subscribe to its 'Software as a Service' platform. Globally, Xero has more than two million subscribers.

Xero's focus on the constantly evolving needs of SMEs also drives its Asia strategy. Reaching these customers and meeting their needs has depended on the relationships it has built with banks, government departments and software developers. Demonstrating a commitment to the region has established its reputation as a market leader in multiple regions. It has also equipped it with the network of collaborators it draws on to rapidly customise its platform to the particular banking, tax and regulatory requirements of SMEs in each market to keep up with technological change.

BEGIN WITH THE SME

Xero applies insights gained from success in its home markets (New Zealand and Australia) to identify opportunities overseas. Kevin Fitzgerald, Xero's Managing Director, Asia, has led Xero's expansion into Singapore, Hong Kong and across Asia. He points out that consumers have the biggest impact on when and how SMEs digitise. In many parts of Asia, it is normal to pay through a QR code or the vast numbers of digital wallets now in common use. The growing popularity of these tools, more than anything else, has driven SMEs' decisions to invest in digitising the point of payment.

Fitzgerald explains that the moment businesses are satisfied that they have adapted their front offices to the demands of their customers, they turn their attention to the back office. "We digitise the back office and then the business realises all the other things Xero can do. It then becomes a wider digital platform when they realise the power of it." Xero had observed this inflection point occurring in Singapore, which in part drove its decision to begin its Asia expansion there.

COMMIT TO MARKET AND BUILD TRUST

Policies to digitise SMEs in Hong Kong and Singapore have enabled Xero to position itself between banks, governments and SMEs as a trusted partner. "We recognised pretty quickly that the banks have a much stronger relationship with SMEs versus anywhere else I've seen in the world," Fitzgerald says. "The banker is still the go-to person for business advice. They go to talk to banks about software. The reason is that Singapore and Hong Kong have a lot of grants to help businesses digitise. But they shift them through the banks. It's a well-controlled and well-oiled mechanism."

Xero was in a strong position as a global market leader to build relationships with banks when it entered the Singapore market. It was quick to launch partnerships with DBS Bank, OCBC, HSBC, UOB and CIMB to enable transactions to flow into their Xero files each day providing real-time information. Xero realised that to convert SME-facing banking partners to advocates for its product, it needed to demonstrate a commitment to the market. As a leader in the kind of technology that the banks and governments need to further digitise, Xero has been able do this by offering itself as a trusted advisor. "We went in with the approach that we can help you understand what you need to do, rather than approaching it as a race to get it done. So we became a consultant to them. In turn, they're talking about us with the SMEs and communicating the message about Xero," explains Fitzgerald.

Building relationships with the developers that make up its API community in Asia relies on a similar dynamic. When Xero entered Singapore, it was seeking to build relationships with developers. It needed to assure them they were investing their resources in a partner that would stay around. Xero now finds that it is being approached by developers across Asia to help it customise its platforms to tax and other requirements across the region.

USE YOUR NETWORKS TO CUSTOMISE QUICKLY

Xero's commitment to building and maintaining partnership networks in Asia is driven by more than the need to build its brand. It also allows Xero to quickly adapt to tax and regulatory requirements to meet the particular needs of SMEs in each market it enters. As an example, payroll is different in each country. Xero has partnered with the leading cloud Payroll/HR partners in each country to ensure local compliance is met; this is where Xero works with the best of breed in each country to localise its product offering. Allowing these partners to focus on their technical solution and partner with Xero brings the SME a powerful cloud solution.

When the Singapore government announced it would be integrating a new e-invoicing system, Xero tapped its developer community and found a solution that could be easily integrated in weeks, ensuring Xero was one of the first companies to apply it. "We went with an ecosystem partner that already had the e-invoicing capability built. Within a matter of two weeks we had completed the beta testing. We worked with them and the government, achieved sign-off and launched."

CASE STUDY

TREASURY WINE ESTATES: BASED ON AN INTERVIEW WITH MATT YOUNG, CHIEF FINANCIAL OFFICER

Over the past five years, Treasury Wine Estates' (TWE) commitment to building premium wines from some of the world's best winemaking regions has seen it evolve into a global business that now sells wine into more than 100 countries.

As the business' global footprint has evolved, TWE has focused on driving growth in Asia and its best-known label – Penfolds – has been at the centre of its success story in the region, particularly China.

Today, TWE is the largest single importer of wine in China thanks to a real commitment to building relationships and developing a deep understanding of its customers and consumers.

GET CLOSE TO THE CUSTOMER

Most wine imported into China is managed by distributors or négociants and sold through a Chinese distribution network, which can limit the wine producer's influence on how its brands are managed and distributed.

CFO Matt Young says TWE's global strategy is to consistently build routes to market that enable it to be as close as possible to the consumer, particularly for its luxury wines, allowing the business to influence how its brands are marketed and priced.

In 2015, TWE made a significant change to its route to market in China, forming direct relationships with Chinese retailers, e-commerce providers and wholesalers. This gave TWE direct access to retailers and paved the way for expansion into further provinces and cities. In 2017, TWE opened its first warehouse in Shanghai, creating more flexibility in how it distributed wine to its new partners.

These decisions allowed TWE to establish closer relationships with wholesalers, retailers and consumers.

Young explains: "Making the decision to establish a more direct route to market has been key to our success in China because we've been able to open up and build new relationships. These relationships have helped us gain a better understanding of the Chinese market and consumers.

"The strategy has also allowed us to invest more in our team on the ground, along with advertising and support for our brands, and in doing so make it easier for Chinese consumers to get to know and enjoy the quality of our wines."

KNOW YOUR INVENTORY

Understanding how to target consumer demand and manage supply chains as seamlessly as possible is critical to the success of any consumer goods business, particularly a wine business which often has longer, and global, supply chains.

Detailed analysis of wine sales and inventory in trade allows TWE to effectively and efficiently allocate luxury wines to markets and customers which are growing, while managing customer stock levels appropriately.

TWE manages this challenge by investing heavily in its own data collection systems. In mature wine markets, TWE can source retail sales data from specialist companies like Nielson.

In China, where this level of monitoring of data by external firms is not yet as sophisticated, TWE collects and analyses data directly from its customers on a monthly basis and employs a third-party firm to undertake audit procedures to check stock levels. Senior leaders of TWE's global business, including Young, visit China periodically to analyse this information in detail and, at times, make inspections.

Young explains that this high level of vigilance comes at a cost, but it enables TWE to identify partners that require additional support, as well as assess the success of its sales strategy and promotional programs.

"This process has allowed us to quickly identify and resolve issues – faster than others in the market."

COMMIT TO MARKET

Growing TWE's presence in China has not been without its challenges.

Young says the challenges have helped the company appreciate the importance of having deep relationships within the market and the need to have a local team with strong operational and sales experience.

"As we've grown in China so too has our commitment to weave ourselves deeper into the fabric of China beyond our relationships with wholesalers, retailers and consumers," he says.

"This includes making sure TWE can attract talent as we grow our team in China, build stronger government and industry relationships and continue to invest in our operational capability, such as opening further warehouses in the future.

"These signal TWE's long-term commitment to China."

Engaging with investors: How the best public company executives inform, educate and engage with their investors on their Asia strategy

Long-term engagement in Asia requires patience from investors. For Australian public companies, the pressure to demonstrate returns over very short periods of time is a potential disincentive to investing in a growth strategy built upon expanding into new markets in Asia. To understand how Australian companies have succeeded despite these pressures, we spoke to senior executives of seven ASX 200-listed companies that have implemented successful expansion strategies in Asia.

Several of the companies we spoke to boast decades-long engagement with Asian markets and all position themselves as established global companies. Their emphasis was on regular communication and making themselves available to investors. We also spoke with companies that had recently listed or recently expanded into new markets in Asia. Their emphasis was on educating investors, especially for those whose product offering was new. All the companies we spoke to agreed that choosing your investors as much as possible was desirable.

Choose your investors

"In the end the investor buys you," said one CEO of a leading healthcare business, but this does not mean, he stressed, that management has no role in selecting investors. "Management's role is to explain the purpose of the company, the strategy of the company and the plans in a logical way that gets investors either on board or has investors saying actually this doesn't suit my investment process and style and I'm not going to invest in this company."

One CFO of a global consumer staples business said: "First you have to know what you as a company stand for, and then pick your investors. Knowing what the range of potential investors are out there and what suits you. Pick them, look after them, target your next group of investors because you have to assume turnover."

All the senior executives we spoke to stressed that they look for investors who perceive their company as a long-term opportunity. One CEO of an international consumer discretionary business said: "They all say they're long-term strategic investors but it takes a while to figure out whether that is truly the case. We spend a lot more time with investors we identify as long-term and we really work hard with helping them understand the business. A lot of work goes into helping investors understand our work.

"Part of our investor relations function is to look for investors that have a process and an outlook that matches with our strategy. We are very clear that our strategy is a long-term strategy. In our business we need to be able to support our customers throughout their lifetime."

This company only looks for investors who seek long-term growth. "If you look at the register, most of the active members are long-term holders, so there's a natural match there. We're selective – you can choose who you meet with to some degree."

Wherever possible, the CFO of a global consumer staples business added, "companies should choose investors who can advise, build connections and create opportunities for you."

Companies generally also sought out international investors. One CEO of an international consumer discretionary business said: "Most of our investors were Australian-based and were institutions. That's slowly changing. We as a team recognise over time we need to build a stronger international investor base." This mirrors the company's evolution from an Australian exporter of services to a company that sources and serves clients from all over the world.

Keep in touch

For the companies we spoke to that have been in Asia for three decades or more, communication with investors is primarily about managing stable long-term relationships. This requires regular communication, generally after half-yearly results, and a policy of making senior executives available to address queries or concerns in between. Regular investor tours of global operations are also typically part of their communication strategies, with more than one senior executive highlighting the importance of also including analysts. One regional CEO of a leading multinational construction, infrastructure, and property business said it is useful to work with other international businesses to organise these tours, and the Australian government plays a useful coordinating role.

For the companies we spoke to that are expanding into new markets, especially with new products that the market is less familiar with, educating investors is the primary concern. Building investor support for a rapidly growing international footprint, especially involving acquisitions, requires companies to demonstrate the opportunity.

One senior executive of a leading construction materials business said it is important to have credibility with your investor group and then the story is about strengthening your position.

The CFO of a global software technology business explained that the company's investor communication strategy is built around educating investors about their products and new market opportunities. "Something that we do particularly well when we are going into a new region is talking about the opportunity we've got within the market and the headroom. Really looking at the total addressable market and also the current penetration in that market. That shows them the huge amount of opportunity that we have and the headroom that we've got to grow in that particular market," she said.

"This part of our investor relations strategy is crucial. Particularly in a company like ours where we are growing so quickly it is important to have regular touch points, not just to update them on any changes in strategy but also to show them we are achieving what we had set out to do. If we're doing something different, if we're acquiring a business, it becomes important to have other touchpoints throughout the year. It takes a lot of time but since we are growing so fast and doing new things all the time it's important that investors know what is important to us and can see that we're hitting those milestones."

One CEO of a leading construction materials business explained they undertake analyst and investor tours in Asia over a one-week period. The yearly site visits are an opportunity to meet the management teams, talk to them about the vision and results along with the strategic priorities. This helps to reinforce the message and gives investors confidence in the management team and the business.

Get the balance right

All companies agreed that clearly articulating long-term strategy is essential to building confidence in the investor community. This has been the experience of long-established players with strong track records as global companies. One CEO of a leading healthcare business said: "I push back on the idea that investors control the strategy of companies. I do think it's a management obligation to articulate it really clearly and garner support. I don't agree when a company says investors have pushed us to deliver short-term results at the expense of long-term results. I bet there is not a shareholder anywhere who says 'please compromise the shareholder value in the long-term to deliver this half'."

One senior executive of a leading technology business sees integrating short and long-term incentives as part of his role as a leader of a company with a fast-growing international footprint. "When you're a public company, you're measured by the share price. Sometimes that's something you can have no direct effect over. The key to it is the creation, maintenance and execution of the strategy," he said.

"You've got to have short-term goals to meet investor and market expectations and our own expectations, but at the same time those short-term goals have to be stepping stones towards the long-term strategy. Sometimes it's challenging to combine the two but that's what we're tasked with as part of our remit as executives in a public company. Part of the job is to balance that and get the incentives right. Especially as a growth business. We want to continue to grow, not just grow for 12 months. We're continually planning that long-term growth."

All the senior executives we spoke to agreed that remuneration of senior executives should reflect the balance between long and short-term goals, and described packages based on meeting short-term targets as well as rewards measured by long-term shareholder returns. "It has to be about balance," said one CFO of a global consumer staples business. "Short-term incentives should reward early good performance in support of a long-term ambition. Make sure you have a range of metrics and incentive structures that are aligned to long-term objectives." This should include profit targets, "but also non-financial targets."

Private companies

CASE STUDY

HURRICANE'S GRILL: BASED ON AN INTERVIEW WITH CRAIG GOLDBERG, MANAGING DIRECTOR

Since opening its first steakhouse at Bondi Beach in 1994, Hurricane's Grill has become a Sydney favourite, with four restaurants now across the city.

Over the past four years, founder Craig Goldberg has taken Hurricane's global, with restaurants opening in Jakarta, Dubai and Beijing. It is now poised to expand across China.

Goldberg relates that as a hospitality brand, Hurricane's connects with a worldly young Chinese demographic that is familiar with western cuisine and excited about an Australian dining experience. Hurricane's can also count on the growing strength of Australia's reputation as a source of high-quality produce, and the expansion of the food and beverage supply chains between the two countries.

BUILD ON BRAND AUSTRALIA

Hurricanes' reputation in Australia is built on its ribs. Goldberg's family has been in the steakhouse business for generations, and his pork rib basting sauce recipe is a well-guarded secret. When he migrated to Sydney from South Africa in 1994, he saw a gap in the market for his barbecue experience. "When I arrived, ribs weren't a big thing in Australia," he explains. "We had butchers saying buy our beef and we'll give you our pork ribs for virtually nothing." In the decades since, the menu has incorporated fresh Australian produce and become a mainstay of the Sydney dining scene. "Over 25 years, we have become an established Australian brand of steakhouse. When people think ribs they think of Hurricane's."

Its growing popularity among Asian tourists and students, and a constant stream of enquiries from overseas about licensing the brand, prompted Hurricane's to open its first restaurants in Indonesia and the United Arab Emirates over the past four years. Most recently, Hurricane's has opened in a fashionable part of Beijing. "There are a lot of students that have studied in Australia and gone back to China, born in the 1990s and 2000s. They are very aware of western tastes and are familiar with Hurricane's. We have whole groups of students who used to study together in Sydney come into Hurricane's in Beijing." Goldberg goes on to explain that this generation in particular "is so much more aware of new and better things through social media, and through studying overseas. Their eyes are wide open to the Hurricane's dining experience and they want it."

Beyond the familiarity of its own brand, Hurricane's can trade off the strength of Australia's reputation, which has grown steadily in esteem over the past decade as brands such as Bellamy's and Penfolds become more available and affordable to Chinese consumers. Since its core offering is its strongest selling point, Hurricane's has not had to change its menus much to cater to local tastes, other than including some local staples and other minor adaptions. "It has been trial and error," Goldberg explains. "We're happy to adapt as long as our core menu stays the same. We do a mango cheesecake in Beijing which is very popular, we do a Mars bar cheesecake in Australia. We want to keep our core values – affordable, quality meals."

Hurricane's is also in a better position than ever to source Australian produce in China. The demand for high-quality imported meat has been growing steadily in China, and as a consequence supply chains have broadened and matured. "We thought it would be really hard. We wanted to know how we were going to get beef to China, how were we going to get alcohol because we really wanted to showcase Australia. But there's already so much supply going into China. I haven't found an issue with supply chain," says Goldberg. He adds that his suppliers have a good integration of cattle in Australia and production in China. "This helps us build efficiencies and have better control over quality." Goldberg also highlights the support from Australian governments and the Australian business community in China. "You have AustCham there. They have so many good connections to people who can point you in the right direction."

PARTNER TO GROW

The growth opportunity China provides Hurricane's is of much larger scale than Indonesia, the UAE or other markets Hurricane's has considered. Hurricane's has set up a joint venture with a Chinese company with experience in hospitality which will give it the means to expand quickly. Goldberg explains: "I'm passionate about the brand. I didn't want to put it into the market and then not get the right exposure. Our plan is to go from one restaurant to maybe a hundred in China."

CASE STUDY

THE SILC GROUP: BASED ON AN INTERVIEW WITH KOBY JONES, MANAGING DIRECTOR

The SILC Group is a specialised financial solutions provider servicing wholesale private, commercial and institutional clients. It offers corporate, capital and portfolio solutions across the full spectrum of investment, lending and financial markets products.

The SILC Group commenced scoping as part of its China market expansion strategy by focusing on Shanghai and Hong Kong in 2013. From 2015, after the analysis stage, it commenced establishing relationships and working with local intermediary advisors and associations in the market.

ESTABLISH RELATIONSHIPS AND THEN FORM PARTNERSHIPS

Koby Jones, Managing Director of The SILC Group says: "Asia is so big you can't not be there! The decision to invest in Asia was not difficult. As a financial services company focusing on wholesale markets, Australia is not large enough and there is a critical need to find new markets."

The company's first visit to China was through a trade mission organised by the Victorian government with a focus on the infrastructure sector. This provided the opportunity to be introduced to different companies and was also a great opportunity to explore the culture, size and appetite of the market. Jones explains that he used this approach to visit China several times through trade missions organised by the Victorian government and Austrade and each time focused on strengthening existing relationships and developing new ones. Once the relationships were firmly established, the company leveraged them to start identifying local intermediary advisors in the market it could partner with.

The SILC Group currently has a network of approximately 20 local intermediary advisors who have access to more than 200 relevant clients in Asia. Partnering with the right intermediary advisor who is trusted, can negotiate, communicate and engage with the local market was essential and key to building a sustainable and successful strategy.

THERE ARE WAYS TO INTERNATIONALISE AND STILL MANAGE YOUR CAPITAL OUTLAY

The business model operates by having a presence in Australia that has a connection to the intermediary advisors in their respective local markets, who in turn have access to the relevant potential clients. The strategy to use only local intermediary advisors has allowed The SILC Group to minimise financial risk and capital outlays. The intermediary advisors in the relevant markets work directly with the local clients. Jones refers to this approach as a soft entry approach that minimises his company's risk exposure and ensures warm introductions. Intermediary advisors get paid a success fee percentage based on the amount invested by their clients. There are no local offices in offshore markets at this stage to keep costs low, but Jones ensures he undertakes regular visits to meet his local advisors. His management team in Australia is also in constant contact with the team in China and Hong Kong and other markets in Asia.

The SILC Group is continuing to invest in technology to offer more products and services to increase its reach as it is not possible to be in all the markets. The focus of the technology is on efficiency by reducing the number of physical touch points, improving velocity by increasing the speed at which responses and engagement can be provided, and enhancing scalability by increasing the reach to cater to a wide range of markets, not only in Asia but globally. As a result, the company has actively been investing in technology to achieve its growth strategy and is collaborating with a major university in Melbourne to develop its platform. Relationships are what matter in these market segments and The SILC Group is using technology as part of the solution, which is combined with a novel distribution strategy. Diversifying and being international can be done with limited capital investment and continuing to maintain a low operational risk profile.

TAKE TIME TO BUILD A PRESENCE AND THEN ACCELERATE

Jones first visited China in 2013 to understand and explore the market and build relationships. From 2015 he started identifying who The SILC Group could be working with and then built partnerships with the local intermediary advisors. The company has grown its presence in Shanghai and in Hong Kong, which is now the hub for the company in North Asia, and also has networks in South-East Asia, particularly in Singapore and Malaysia. The SILC Group also has connections in Beijing and Guangzhou and has explored 11 cities in total in China.

COVID-19 has fortunately not impacted the business. Instead, it has grown its client base during this period, given their focus is on alternative assets and wholesale investors who are mature in their outlook and are focused on long-term outcomes. Alternative assets are gaining more interest and popularity with the firm's client base in Asia. Within alternative assets The SILC Group is attracting investment from clients in Asia related to private debt, private real estate, private equity, infrastructure and agriculture. The current environment has produced a positive outcome for the business, as Jones explains there is also a rapidly growing middle-class in Asia that is demanding more access to and choice in these solutions.

He says Australia has a strong reputation as a well-regulated, transparent, stable and trusted destination for capital, and The SILC Group needs to be ready to provide its services and solutions to clients. "There is a market for it in Asia and we need to strongly engage as it is no longer going to be optional, but essential for our long-term sustainability. Asia is the future and it is right on our doorstep ready to engage."

Why private companies are so successful in Asia: Understanding the factors that drive their success

As the case studies above highlight, private companies have a fundamentally different set of factors that drive strategy, decision-making, and long-term commitment.

Our consultations with some of Australia's leading private company executives and board members highlighted three key themes underlining private company success in Asia.

Family-based relationships are key

The history and continuing strength of family-owned companies in Asia is well documented. Across South Korea, China, India and South-East Asia, family-owned companies have a long history of dominating commercial activities across sectors, dominating national development agendas, and going global.

> *"Australian family companies on balance are going to do better in an economy where your counterparts are families. So, it's not that Australian private companies are better placed, it's that Australian family companies have done quite well overseas because they have tended to have family relationships. We should not underestimate the culture of Asian companies which are heavily biased towards family companies."*
>
> Peter Yates, Deputy Chair, AIA Australia Limited and Non-Executive Director, Linfox (stakeholder consultations)

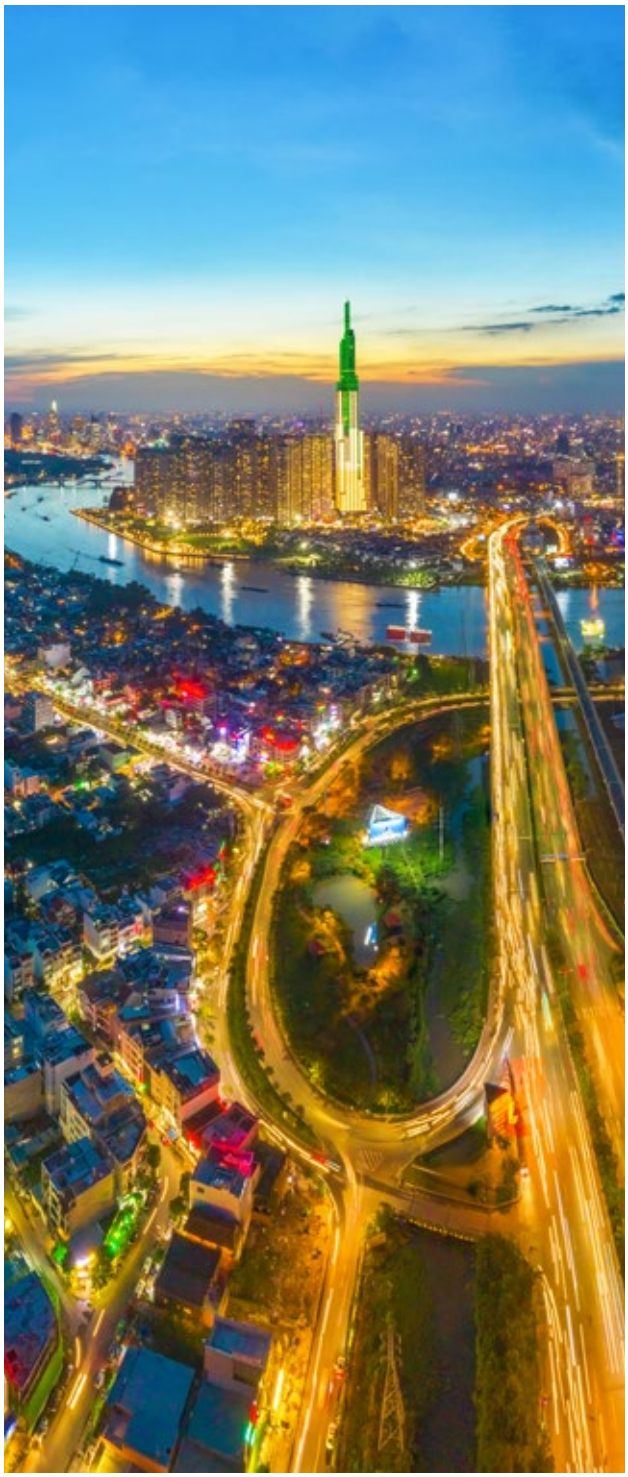
Long-term orientation

The long-term orientation of private companies, in particular family-owned companies, has been critical to their success in Asian markets. This long-term orientation is often attributed to the longer tenures that board members and senior executives have in family-owned companies.

> *"Private companies do have more time and do care more about the building of personal relationships with their business partners. Private companies are owned by people and those people are not going anywhere because they own the company. In the public company world, the movement of executives and talent means the relationship you build with one person may not last long because that person will end up doing something else somewhere else conceivably in the same company or another one."*
>
> Sid Myer, Chair, Myer Family Investments (stakeholder consultations)

Patient capital

Our consultations highlighted the capability of family-owned companies to deploy patient capital. Patient capital enabled the pursuit of truly long-term strategic investments. Our research has indicated that many Australian family-owned companies typically look at investments and their associated returns in much longer time frames than Australian listed companies.



"Continue to press and encourage the use of the term patience. Patience is an important part of the DNA of successful business people and successful organisations who have made a success of building a presence in Asia."

Sid Myer, Chair, Myer Family Investments (stakeholder consultations)

" Private companies have an advantage in building new markets including in Asia and the primary advantage is not being beholden to the cycles of reporting and other statutory requirements of public companies. The ability as a result to think long-term about the way in which they enter new markets is a great advantage."

Sid Myer, Chair, Myer Family Investments (stakeholder consultations)

"Private companies because they look at the long-term strategy may not be quite as focused on the short-term returns as public companies which are focused on their Return on Equity.

"Private companies and family-owned companies also tend to be more focused on the strategic dividend (capital growth) rather than being earnings accretive (short-term)."

Peter Yates, Deputy Chair, AIA Australia Limited and Non-Executive Director, Linfox (stakeholder consultations)

Match Fit 2.0: Creating Asia-capable leaders

MATCH FIT 2.0: CREATING ASIA-CAPABLE LEADERS

By Mukund Narayanamurti, Chief Executive Officer, Asialink Business
with the support of the AICD

INTRODUCTION

World economic weight continues to shift rapidly towards Asia. To succeed in the biggest and most dynamic markets in our region, Australian companies need to compete for consumers, capital and talent. As Asian markets recover from the COVID-19 pandemic, business leadership that understands the need to build knowledge and skills relevant to operating in Asian markets is more urgently needed than ever.

To measure these qualities in Australian business leaders, Asialink Business has developed a methodology to capture the experiences of ASX 200 board members and senior executives. Collection of data on these experiences, which cover Asia-related work experience and work experience in Asian markets as well as linguistic capability and educational background, enabled us to measure the six Asia capabilities individuals need to build successful business relationships in Asia. This section analyses individual capabilities and provides an overall Asia capability score for 1,705 board members and senior executives of ASX 200 companies (as of 1 January 2020).

In summary, our findings highlight the following:

1. **Asia capability among Australian business leaders remains low**

In 2017, Asialink Business[43] released *Match Fit: Shaping Asia-capable leaders*, a report which measured the individual Asia capabilities of senior executives and board members of ASX 200 companies.

Three years on, our research finds that Asia capability among senior leaders of the ASX 200 has not improved. The average Asia capability scores for board members and senior executives are 13.8 per cent and 13.5 per cent respectively. Importantly, only seven per cent of board members and senior executives would qualify as Asia-capable (that is, have a score greater than 50 per cent). This means that over 90 per cent of senior leaders (board members and senior executives) in the ASX 200 would not qualify as Asia-capable. These results are concerning as our research has consistently found that companies with an above average level of Asia capability in their senior leadership generate a greater proportion of their revenues from Asia.

We did find that the vast majority of board members and senior executives, however, had worked for companies that export goods or services internationally. This suggests that while most business leaders possess the general skills to work across borders, few have the specific Asia skills necessary to fully capitalise on opportunities in Asia.

2. **Business leaders perform highest on market knowledge and lowest on cultural understanding**

We found that leaders were, on average, strongest in their knowledge of Asian markets and weakest in their ability to adapt to Asian cultural contexts. This suggests that while Australian business recognises the need to understand the market opportunity presented by Asia, this knowledge is not yet matched by an appreciation of the cultural skills needed to execute on those opportunities.

3. **There is a small cohort of leaders with high Asia capabilities that can enable their companies grow their exposure**

We found that financials, consumer staples and materials were the sectors with the highest number of Asia-capable board members and consumer discretionary, materials, financials and consumer staples had the highest number of Asia-capable senior executives.

What these results indicate is that, subject to industry dynamics, there is significant upside potential in our consumer staples and consumer discretionary companies assessing and executing opportunities with Asian markets. They are underweight with their international exposure while they have amongst the highest number of Asia-capable senior leaders.

Our materials and diversified financial companies are already strong with their international exposure. Our banks and insurance companies are very low with their international exposure but they have had significant experience already in evaluating opportunities with Asian markets across a range of products and services. The value of Asia-capable senior leaders to our banking and insurance sectors may lie in their understanding of international best practice in governance, risk management, technology, and management.

The results indicate that for as long as we remain export-driven in commoditised sectors the relative need for Asia capabilities in board and senior executive teams may be lower. As we transition to more outbound investment, typically in more services driven sectors, the relative value of Asia capabilities will increase. Consequently, as we seek to export a greater proportion of services to the Asian region, Asia-capable senior leadership will be critical to successful offshore expansion.

Our consultations with senior leaders have highlighted several constraints impacting the pursuit of long-term opportunities with Asia. These include the increase in geostrategic risks, significant growth in expectations on boards, low risk appetite in a low-growth environment, a lack of Asia-capable leadership and negative public perceptions.

Our consultations have also revealed several key recommendations to improve the level of Asia capabilities in senior leadership teams. These include identifying, recruiting and retaining Asia-capable leadership, taking a strategic approach to engagement with Asia, building awareness through evidence rather than anecdotes, and creating a tripartite agreement between business, peak bodies (such as the AICD) and government to make the low levels of Asia capabilities on boards a strategic priority.

A BESPOKE METHODOLOGY TO MEASURE ASIA CAPABILITY

The Asia capability assessment is a bespoke methodology that was developed by Asialink Business to assess an individual's ability to operate in a business context in Asia.

The 2012 Asialink Taskforce[44] defined 11 Asia capabilities that contribute to an organisation's ability to compete in Asia. Six of these capabilities apply to individuals and five to organisations[45].

TABLE 4. ***The 11 Asia capabilities***

INDIVIDUAL CAPABILITIES	ORGANISATIONAL CAPABILITIES
Sophisticated knowledge of Asian markets/environments	Leadership committed to an Asia-focused strategy
Extensive operating experience in Asia	Customised Asian talent management
Long-term trusted Asian relationships	Customised offering/value proposition based on customer insights
Ability to adapt behaviour to Asian cultural contexts	Tailored organisational design with tendency towards local autonomy
Capacity to deal with government	Supportive processes to share Asian learnings
Useful level of language proficiency	

As highlighted in previous research by Asialink Business[46]:

- Asia is not a single, homogeneous market. As a result, individuals may be Asia-capable in the context of a single market or several.
- Asia capabilities are not dependent on Asian ethnicity and neither are the two mutually exclusive.

The methodology designed for this study focused on the six individual capabilities of ASX 200 leaders (board members and senior executives) to understand how well-placed ASX 200 companies are to take advantage of emerging opportunities in Asia.

To objectively measure the Asia capability of ASX 200 leaders, Asialink Business collected data on 10 metrics related to each leader's study and professional experience. Each of these metrics was then mapped to the six individual Asia capabilities (**Table 5**).

TABLE 5. *10 experience metrics to measure individual Asia capabilities*

EXPERIENCE METRICS	DATA COLLECTION
Responsible for Asian markets	Checked CV for international marketing role or role specific to exports to or serving clients in Asian countries
Worked in Asia	Checked CV for any period of work in Asia
Worked in Asia in a senior position	Checked CV for position of manager, director, executive or higher level in Asia
Worked in Asia for more than two years	Checked CV for any period(s) of work in Asia totalling over two years
Worked in Asia for more than five years	Checked CV for any period(s) of work in Asia totalling over five years
Pre-university study experience in Asia	Checked CV for high school level education experience in Asia or description of early life
University level study in Asia	Checked CV for degrees or certificates in Asian universities
Studied an Asian language or Asian studies	Checked CV for any majors/minors in Asian study in education section
Fluent in an Asian language	Checked skills section in CV for Asian language study or evidence of living in non-English speaking Asian country from a young age in which they would very likely be speaking an Asian language
Worked for exporting company or company with overseas presence	Checked CV for experience in multinational company or company that exports to any country

The experience metrics were collected as binary data (yes/no) to reduce the subjectivity inherent with a scale. Data was also collected on role, gender, sector and geographic markets served. The data was sourced from LinkedIn Premium, Bloomberg, company and other relevant websites, and annual reports. All data was de-identified to ensure anonymity of individuals was maintained.

A panel of 18 experts with significant Asian business experience was surveyed to map the importance of each metric to the six individual Asia capabilities. Each experience metric was weighted differently depending on its relevance to each of the six individual Asia capabilities; the weights were determined using the results of the expert survey responses.

Each person's overall Asia capability score was expressed as a percentage of the total points available across all individual capabilities.

While the methodology was designed to minimise its limitations (for example, data restrictions and subjectivity), it is important to interpret the results in light of the following:

- Some of the LinkedIn profiles were incomplete but this was a minor limitation given the large sample size and the amount of individual data available due to the companies being listed; and
- The weighting of the importance of different experiences to Asia capability is quite subjective. To reduce the subjectivity, we surveyed 18 experts with significant business experience in Asia and used the survey averages for the weightings.

ON AVERAGE, ASX 200 LEADERS HAVE LOW ASIA CAPABILITY

On average, both ASX 200 board members and senior executives displayed a low level of Asia capability (**Figure 27**). The average Asia capability score was 13.8 per cent for ASX 200 board members, and 13.5 per cent for senior executives (see **Table 6**). Seven per cent of ASX board members and six per cent of senior executives received an Asia capability score of zero across all experience metrics (see **Table 7**).

FIGURE 27. *Histogram of overall Asia capability scores for ASX 200 leaders*

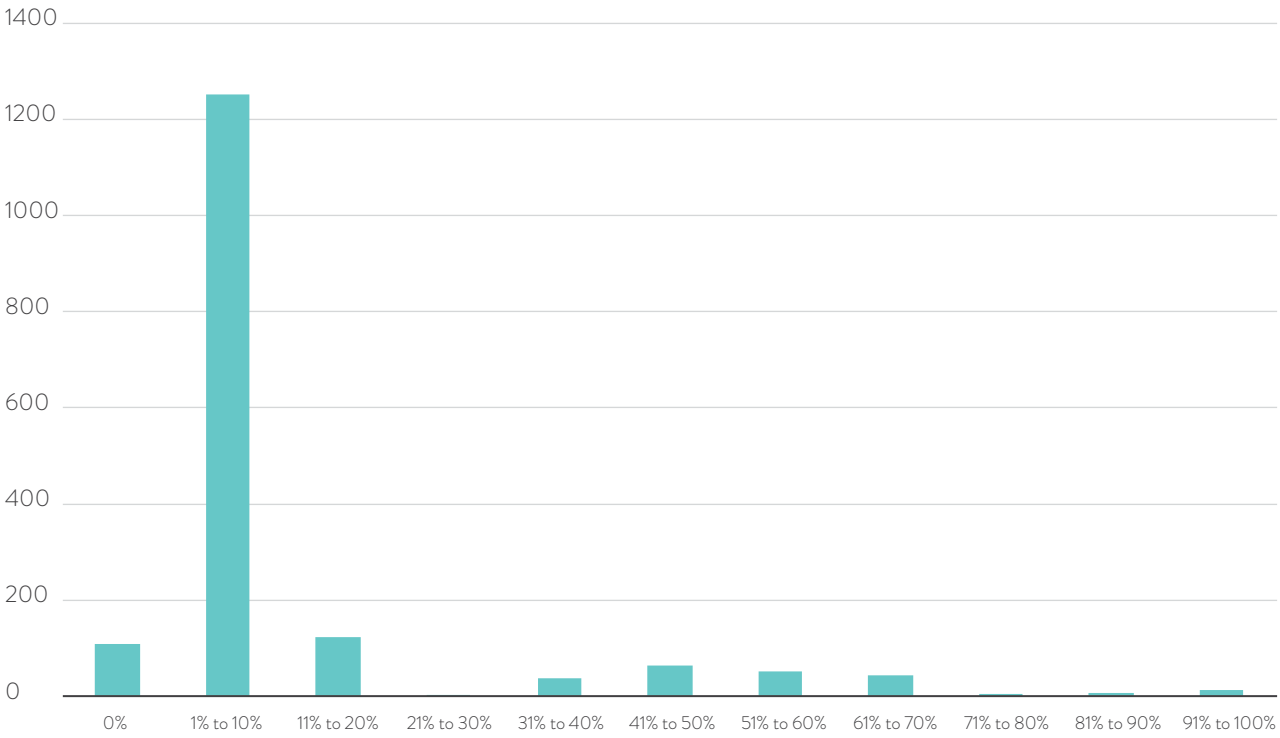


TABLE 6. *Average overall Asia capability score for ASX 200 board members and senior executives (percentage of total possible score)*

	ASIA CAPABILITY SCORE	N
Board Members	13.8%	1438
Senior executives	13.5%	267

TABLE 7. *ASX board members and senior executives who have no Asia capability (number and percentage)*

	ASIA CAPABILITY SCORE OF ZERO (%)	N
Board Members	7%	94
Senior executives	6%	15

Despite low overall Asia capability scores among ASX 200 board members and senior executives, the assessment identified some areas of strength on specific Asia-related experience (outlined in **Table 8** below).

The majority of ASX 200 board members and senior executives (93 per cent for both) have worked for an exporting company or company with an overseas presence, and more than one-in-six have held specific responsibility for Asian markets. This suggests that these leaders have the potential to leverage both their specific knowledge of Asian markets, and broader international outlook to pursue opportunities in Asian markets.

Only a very small proportion of ASX 200 board members (one per cent) and senior executives (one per cent) demonstrated fluency in an Asian language, and almost none had pursued studies specific to Asia or Asian languages.

TABLE 8. *ASX 200 board members and senior executives by Asia-related experience (number and percentage)*

	BOARD MEMBERS		SENIOR EXECUTIVES		TOTAL	
	N	%	N	%	N	%
Responsible for Asian markets	238	17	46	16	284	17
Worked in Asia	196	14	39	14	235	14
Worked in Asia in senior position	159	11	29	11	188	11
Worked in Asia more than two years	114	8	27	10	141	8
Worked in Asia more than five years	53	4	14	5	67	4
Pre-university study in Asia	15	1	5	2	20	1
Fluent in Asian language	16	1	3	1	19	1
Studied an Asian language or Asian studies	6	0	0	0	6	0
University study in Asia	19	1	5	2	24	1
Worked for exporting company or company with overseas presence	1338	93	251	93	1591	93

Using this data on experiences to calculate the six Asia capabilities of board members and senior executives, we found that there was little variation across Asia capabilities among board members and senior executives or on a gender basis (see **Table 9**). We found that men and women, board members and senior executives were on average strongest in their knowledge of Asian markets and weakest in their ability to adapt to Asian cultural contexts. This suggests that while Australian business recognises the need to understand the market opportunity presented by Asia, this knowledge is not yet matched by an appreciation of the cultural skills needed to execute on those opportunities.

TABLE 9. *ASX 200 board members and senior executives by Asia capability (percentage), and by gender (percentage)*

	Knowledge of Asian markets	Extensive experience operating in Asia	Capacity to deal with Asian governments	Ability to adapt to Asian cultural contexts	Long-term trusted Asian relationships	Useful level of Asian language proficiency
Board	15.2%	14.1%	14.3%	11.7%	13.5%	14.1%
Executives	15.5%	14.4%	14.7%	12.1%	12%	12.3%

MEN	Knowledge of Asian markets	Extensive experience operating in Asia	Capacity to deal with Asian governments	Ability to adapt to Asian cultural contexts	Long-term trusted Asian relationships	Useful level of Asian language proficiency
Board	15%	14%	14%	12%	14%	14%
Executives	15%	14%	14%	12%	14%	14%

WOMEN	Knowledge of Asian markets	Extensive experience operating in Asia	Capacity to deal with Asian governments	Ability to adapt to Asian cultural contexts	Long-term trusted Asian relationships	Useful level of Asian language proficiency
Board	15%	14%	14%	12%	13%	14%
Executives	17%	16%	16%	13%	15%	16%

ASX 200 LEADERS BUILD ASIA CAPABILITY IN-MARKET

Asialink Business undertook additional analysis of the results of seven per cent of ASX 200 board members and senior executives who were considered Asia-capable (scored more than 50 per cent) (see **Table 10**). Among this group of Asia-capable ASX 200 leaders, the average Asia capability score was 67 per cent, and 18 leaders (or one per cent of leaders) had scores above 80 per cent.

Previous Asialink Business research has found that 80 per cent of companies that have board members and senior executives with an above average level of Asia capability derive more than 40 per cent of their revenue from Asian markets[47]. Having Asia-capable leadership can also enable more effective decision-making, risk management and innovation, and is particularly important for senior executives who play a role on the ground in Asia-relevant transactions.

TABLE 10. *Average overall Asia capability score for ASX board members and senior executives who have a score above 50% (number and percentage)*

	BOARD MEMBERS	SENIOR EXECUTIVES	TOTAL
Ave. Asia capability score for leaders with a score >50%	66%	69%	67%
n (Asia capability score for leaders with a score >50%)	100	18	118

The analysis revealed a number of trends in the experiences of Asia-capable ASX 200 leaders. Most Asia-capable ASX 200 board members and senior executives have developed their Asia capabilities in their workplaces, rather than through post-secondary study. While few Asia-capable ASX 200 leaders spoke an Asian language or had formal qualifications related to Asia, almost all (98 per cent of board members and 100 per cent of senior executives) had been responsible for Asian markets (see **Table 11** below).

Importantly, on the ground experience is a universal characteristic among Asia-capable ASX 200 leaders. Almost all Asia-capable ASX board members and senior executives had worked in Asia in a senior position, and the majority (53 per cent of board members and 67 per cent of senior executives) had worked in Asia for more than five years. More than a sixth of Asia-capable board members (17 per cent) and more than a fifth of senior executives (22 per cent) completed university studies in Asia – significantly above the overall number of 1.4 per cent.

TABLE 11. *Highly Asia-capable ASX 200 board members and senior executives by Asia-related experience (number and percentage)*

	BOARD MEMBERS		SENIOR EXECUTIVES	
	N	%	N	%
Responsible for Asian markets	98	98	18	100
Worked in Asia	100	100	18	100
Worked in Asia in senior position	98	98	18	100
Worked in Asia more than two years	100	100	18	100
Worked in Asia more than five years	53	53	12	67
Pre-university study in Asia	14	14	4	22
Fluent in Asian language	15	15	2	11
Studied an Asian language or Asian studies	3	3	0	0
University study in Asia	17	17	4	22
Worked for exporting company or company with overseas presence	99	99	18	100

We found that financials, consumer staples and materials were the sectors with the highest number of Asia-capable board members and consumer discretionary, materials, financials and consumer staples had the highest number of Asia-capable senior executives (**Table 12**).

TABLE 12. *Sectors with the highest number of board members and senior executives (number and percentage)*

SECTOR	ASIA-CAPABLE BOARD MEMBERS		ASIA-CAPABLE SENIOR EXECUTIVES	
	N	%	N	%
Consumer discretionary	11	11%	5	25%
Consumer staples	12	12%	3	15%
Energy	11	11%	1	5%
Financials	19	19%	3	15%
Healthcare	7	7%	0	0%
Industrials	10	10%	1	5%
Information technology	4	4%	1	5%
Materials	12	12%	4	20%
Real estate	8	8%	0	0%
Telecommunications	6	6%	0	0%

At board level, Asia-capable leaders were fairly evenly distributed on market capitalisation of the companies that employed them. Large cap and medium cap companies both account for 37 per cent of Asia-capable board members, with small cap companies accounting for 29 per cent. Mid cap companies had the highest number of Asia-capable senior executives at 45 per cent of the total, followed by large cap at 25 per cent and small cap at 15 per cent.

TABLE 13. *Distribution across large cap, mid cap and small cap (number and percentage)*

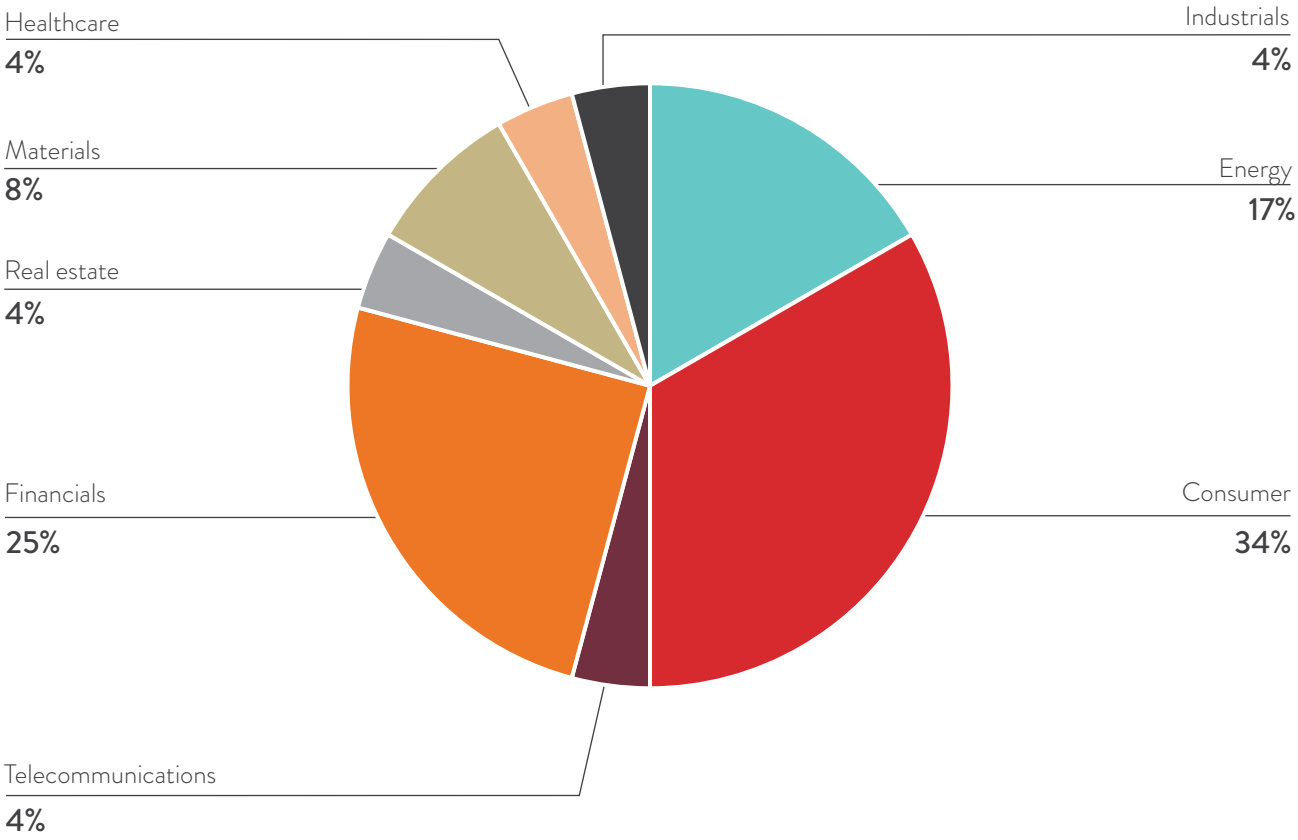
MARKET CAPITALISATION	ASIA-CAPABLE BOARD MEMBERS		ASIA-CAPABLE SENIOR EXECUTIVES	
	N	%	N	%
Large cap (>$10b)	36	37%	5	25%
Mid cap ($2-10b)	36	37%	9	45%
Small cap (<$2b)	28	29%	4	20%

CONSUMER GOODS AND FINANCIAL COMPANIES PERFORMED BEST

A total of 24 companies had two or more board members or senior executives with Asia capability scores over 50 per cent.

Consumer goods was the largest sector represented among companies with more than one board member or senior executive with Asia capability over 50 per cent, making up a third. They were followed by financial, energy and materials companies. There was one company each in the real estate, industrials and healthcare sectors (see **Figure 28**).

FIGURE 28. ***Companies with more than one board member or senior executive with Asia capability over 50 per cent by sector***



WHAT DO THE RESULTS REALLY MEAN? WHAT'S HOLDING US BACK?

As previously stated, Asialink Business' research to date has highlighted both the opportunities with Asia and the relationship between Asia capabilities and superior financial performance. Nevertheless, our most recent consultations with senior leaders have revealed several major constraints impacting the pursuit of long-term opportunities with Asia.

1. Significant increase in geostrategic risks

The impact of COVID-19, the US-China trade war, diplomatic tensions with China and regional security tensions all create a picture of extreme risks for Australian company boards and senior executives. The pandemic has created supply chain disruptions, a depressed business outlook, and employee layoffs.

> *"There is increased focus on non-financial risks including reputation and country risks and geopolitical uncertainty. There is also an increased focus on risks such as political and sovereign risk and bribery and anti-corruption. For example, Indonesia should be a country that Australian companies are focused on; it is one of our closest neighbours with a huge market and significant GDP growth over the last 10 years. Yet boards and senior management remain wary of investing in Indonesia because of concerns about the legal system, bribery and corruption."*
>
> Nicola Wakefield Evans, Non-Executive Director, Macquarie Group, Lendlease, BUPA and AICD (stakeholder consultations)

2. Expectations on senior leaders have multiplied

The Hayne Royal Commission has fundamentally changed the lens through which boards view risk. Australian listed company board requirements are among the most demanding when compared to other jurisdictions. The capacity of senior leaders, particularly in financial services, to consider opportunities in offshore emerging markets has been dramatically impacted.

> *"In the financial services sector the more regulators deliberately start blurring the distinction between governance and management, the more boards are going to go for subject matter experts and specialists to sit on the boards. At one level that is entirely understandable, and you want to have a critical mass of specialists on any board. What it tends to do though is it narrows the overall skills mix of the board and in the financial services sector it is getting to be quite a constraint."*
>
> Peter Varghese, Chancellor, University of Queensland (stakeholder consultations)

3. Low risk appetite in a low-growth environment

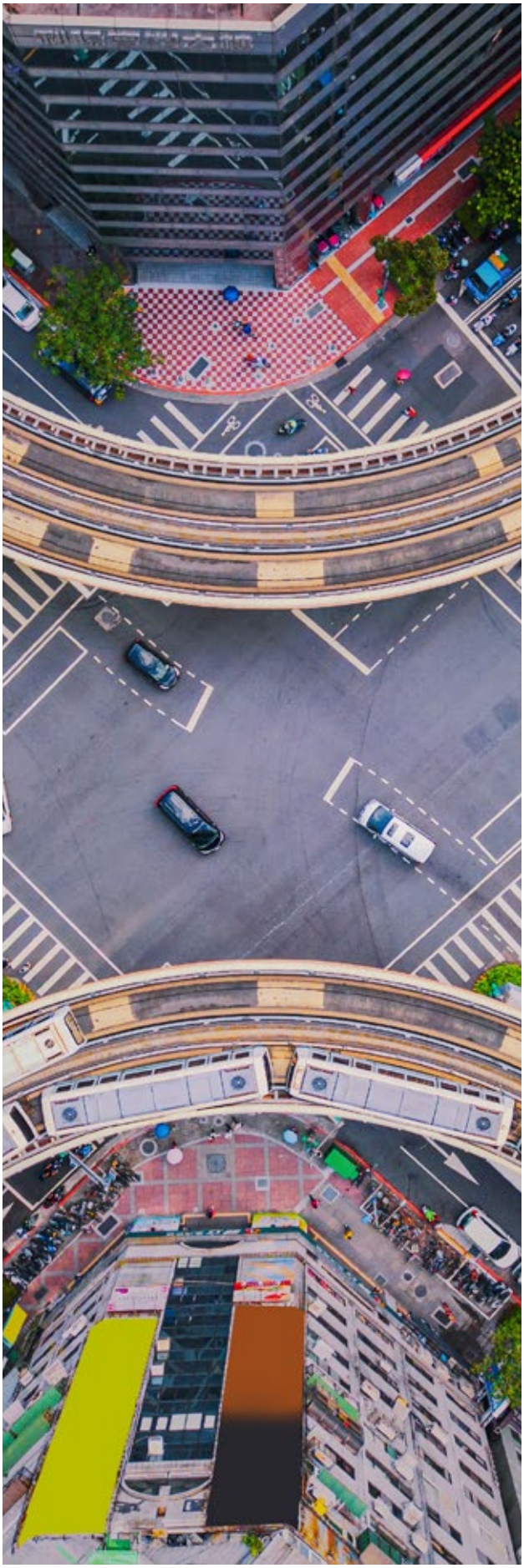
The last three years has confirmed the low-growth environment for corporates. Short-termism continues to be on the rise. Risk aversion among investors also appears to be on the rise. A focus on quarterly, half-yearly and annual performance continues to dominate the attention of senior leaders. Our consultations highlighted the overwhelming desire to focus domestically in the current environment rather than court risks offshore.

"First, the cost of capital to launch overseas compared to funding the domestic business will be significantly greater now due to the perceived risks. Second, a lot of boards are shaken by COVID. Risk maps are now key. There is a risk lens rather than a growth lens. Third, practically it is very hard to get trade done."

Christine Holgate, Managing Director & Chief Executive Officer, Australia Post and Chair, Australia - ASEAN Council (stakeholder consultations)

"Long-term attitude of Australian institutional investors is that you can't be successful in Asia and public companies have worn that quite a lot and then you see private companies and family companies being successful in Asia. This has partly been spurred along by the fact that when investing in Asia, you nearly always are going to have to have a strategic dividend rather than an earnings accretive dividend."

Peter Yates, Deputy Chair, AIA Australia Limited and Non-Executive Director, Linfox (stakeholder consultations)



4. Lack of Asia-capable senior leadership

Diversification and growth strategies determine market prioritisation. Our research identified senior executive leaders responsible for Asian markets who are also responsible for European and/or Latin American markets. They were very effective in certain markets in those regions but naturally not equally effective across markets/regions. Given the heterogeneous nature of Asian markets, senior leaders with country-specific experience are essential.

"There is not a lot of strong conscious effort to have Asia capabilities on boards. ASX listed companies have people leading their Asia markets who may not necessarily have Asia capabilities. They may have experience in other western international markets, but those skills are not necessarily transferable. Having Asia capabilities matter and knowing how markets in Asia differ is critical."

Kee Wong, Non-Executive Director, Carsales and AICD (stakeholder consultations)

5. Public perception

Investor sentiment, media sentiment and broader community sentiment doesn't always support international expansion. A lot is often made of sell-side analysts' aversion to expansion into Asia. This can have an impact on media sentiment, which can just as heavily be influenced by the risk aversion expressed by boards and senior executive teams. The broader community may not also always understand sectors such as energy, FMCG and healthcare, and the impact that international business could have on domestic supplies and local prices.

"Benefits of international investment are not well understood. Companies who have not got it right overseas tend to get more press. We need to talk about more companies that have been successful and get them press time, talk about their story, what they did to get it right and be successful. Australia is a successful economy from a GDP perspective, but we are only 25 million people and will never be in the world's top biggest economies. It is important to understand that."

Ajay Bhatia, Managing Director - Australia, Carsales (stakeholder consultations)

"The way that the share price reacts to the analyst communities and media that follow public companies, has an impact again on them to think long-term in developing new markets."

Sid Myer, Chair, Myer Family Investments (stakeholder consultations)

RECOMMENDATIONS

Our consultations with senior leaders highlighted a strategic approach to overcoming the constraints.

1. Identifying, recruiting and retaining Asia-capable leadership

Our consultations have revealed a continuing gap between the roles of nomination committees, in-house talent functions and executive search firms. Who is responsible for creating a new vision for boards and senior executive teams that incorporates global experience and mindset? The best organisations seek global experience and Asia capabilities, not just for an Asia role but for any senior role as they are seeking individuals who can enable them to think globally on geopolitics, technology, management practices, risk management and industry dynamics.

"One of the great values of international engagement in a corporate sense is that it broadens out your horizon and gets you to start looking at what you do as a company, if not in global terms then certainly more in international terms than purely having an Australian domestic market focus. When you start down that track, you inevitably start trying to identify what is international best practice in your particular sector and how you position yourself to be at the right end of that international best practice."

Peter Varghese, Chancellor, University of Queensland (stakeholder consultations)

"Ideally boards should look for directors who understand Asia at the broader geopolitical landscape, economic and social system level. There needs to be a subtle interplay of styles, interactions, high-level thinking and sophisticated debate for good decisions to be made at the board level."

Yasmin Allen, Non-Executive Director, Cochlear, Santos, ASX and Chair, Advance, Faethm.ai and DSO (stakeholder consultations)

"Asia-capable is not just about being able to speak a particular Asian language, it is about being able to navigate the local system and being comfortable with dealing with people from that culture."

Nicola Wakefield Evans, Non-Executive Director, Macquarie Group, Lendlease, BUPA and AICD (stakeholder consultations)

"Having an international board and executive team helps. It is about having the right capabilities and experience. This diversity also allows thinking about internationalisation."

Ajay Bhatia, Managing Director - Australia, Carsales (stakeholder consultations)

2. Taking a strategic approach to engaging with Asia

Our consultations revealed that the best companies take a structured long-term approach to engaging with Asian markets. This typically includes active involvement of the board through multiple visits to the region, hiring local talent, engaging with government (host and home country), and industry bodies and advisors to navigate opportunities and risks with the new market.

"As expected with business in Asia there are lots of bumps along the road. Success is often the result of the board understanding the opportunity, hiring local talent with knowledge of the market, and complementing it with others who understand the context of an Australian listed company doing business in the region."

Christine Holgate, Managing Director & Chief Executive Officer, Australia Post and Chair, Australia - ASEAN Council (stakeholder consultations)

3. Building awareness through evidence rather than anecdotes

Anecdotes on the challenges of doing business in Asia abound in the Australian corporate sector. Outdated views of markets, government policies and the ease of doing business are not uncommon. In dynamic, high-context Asian markets (from Japan to India), data that is often more than 12 months old can be redundant. The pace, scale, breadth and depth of a large number of Asian economies necessitates research and analysis that is current.

Supporting contemporary research and analysis with time spent on the ground is vital to validate research findings. The very best companies often require board members to join senior executives on visits to key markets.

"While there might be concern on how we engage with those markets and the risks, if you have the right advisors and the right partners the risks can be navigated as it can be navigated in any market. But it does take skills and expertise and more specialist expertise in the area, especially if you don't speak the language or understand the regulatory or policy frameworks."

Sue MacLeman, Chair, MTPConnect , Anatara Lifesciences, Tali Digital Ltd, and Non-Executive Director of Palla Pharma Ltd, Oventus Medical Ltd, and Veski (stakeholder consultations)

4. A tripartite commitment (government, peak bodies and business being committed)

Our consultations revealed a strong appetite for coordinated action to shift the thinking of corporate Australia towards improved engagement with Asia. A transformation of the capabilities of board members will ultimately depend on significant commitment from a range of stakeholders including corporate boards, government and peak bodies. Cooperation and cross-sector collaboration supported by the Australian Government will be critical in ensuring that the development of Asia capabilities becomes a strategic focus for boards.

A multi-disciplinary approach could include initiatives aimed at monitoring progress of Asia capability in leadership, the creation of capability and development opportunities for business leaders, and a cross-sector campaign aimed at highlighting the business case and growth opportunities for Australian businesses. Building on these recommendations, the AICD and Asialink Business will work together to identify further opportunities to increase Asia capability on boards.

> *"The reason you have conversations around the board table is because people are capable, have the experience, the voice, gravitas and the interest in Asia. They also need to have influence to action otherwise it will lead to a missed opportunity. Engaging with Asia needs a thoughtful and considered approach. Having people with understanding, experience, knowledge and passion for the market is essential at both board and executive levels."*
>
> Kee Wong, Non-Executive Director, Carsales and AICD, (stakeholder consultations)

WESFARMERS' APPROACH TO ENGAGEMENT WITH ASIA –

Based on an interview with Diane Smith-Gander, Non-Executive Director, Wesfarmers

Wesfarmers went through a different process to assess the market opportunity and what their supply chain presence should look like and be in Asia.

An element of this involved the entire board visiting Asia twice. The board engaged with Austrade, DFAT and met with ambassadors on the ground. Held government and local community engagement consultations, including significant conversations with other Australian companies that were in the market. Visited sites of suppliers and potential suppliers to get a good feel of the market. They leveraged Australian business partners (such as banks, lawyers etc) by visiting their people in the local offices in Asia and got them to provide information on the potential risks and opportunities in the market.

Prior to even undertaking the above work Wesfarmers identified very experienced local staff that were highly respected and known to the organisation including the board and gave them enough resources to undertake market scans. This was not done over six weeks; this was done over three years.

Over the period Wesfarmers divisions made decisions to significantly raise their investment level. This was only possible because Wesfarmers had an ecosystem of various partners that work was outsourced to. Detailed investigation was undertaken to understand what the right business model would be. Wesfarmers divisions used a blended approach of hiring local people on the ground and rotating team members from Australia into the local market. Those teams and activities are still operating. Because of the in-market presence it positively changed the supply chain profile for Wesfarmers across divisions.

Wesfarmers have been sourcing out of Asia for a very long time. There was an understanding of preventing currency risk, thinking and incorporating ethical sourcing and making sure it was all embedded. It has now become part of the fabric of how the organisation operates.

Wesfarmers has learnt so much when it comes to supply chains from Asia because the ethical sourcing ecosystem is so well developed across Asia. Wesfarmers made changes to the way they thought about their supply chains in Australia as a result of that. Wage issues and product safety issues that were later seen in Australian supply chains had not been such an issue for Wesfarmers because they had already strengthened their supply chains based on their Asian experiences previously. Wesfarmers still has significant offices in Bangladesh, India and China. Wesfarmers continues to rotate their Australian staff through those offices for leadership experiences. Wesfarmers' investment in Asia is continuing to grow.

There are not just trade and investment opportunities in Asia; there are also learnings from very sophisticated companies who operate there.

ASIA-CAPABLE AUSTRALIAN EXPATRIATES – AN INVALUABLE POOL OF SENIOR LEADERSHIP TALENT

Based on an interview with Melanie Brock, Chief Executive Officer, Melanie Brock Advisory Ltd. and Global Ambassador, Advance

As the AFR reported in June 2019, "Melanie Brock has achieved a rare double, becoming one of the few foreigners, and even fewer women, appointed to a listed company board in Japan". Brock was appointed as a non-executive director to the board of Sega Sammy Holdings in June 2019.

Brock has 30 years of experience living and working in Japan. She is one of Japan's most respected APAC specialists. As the AFR reported: "Brock has been a champion for women in business and in recent years has advised Macquarie Group, Crown Resorts, and Tanarra Capital." She is a Global Ambassador of Advance, the trusted platform that connects global Australians with one another and with Australia.

As her profile with Advance highlights, Brock "uniquely combines practical commercial business leadership and language skills to consistently deliver on business, regulatory and partnership outcomes for Japanese and foreign corporations both on global and domestic levels. She has an excellent network in Japan's corporate, political and government sectors".

Brock brings exceptional insights on doing business with Japan. She offers a refreshingly positive approach to engaging with Japan.

> "For too long we have been saying Asia is too hard. We need to shift the narrative away from the notion that 'Japan is simply too hard', to one where we start looking at how we should evolve processes to deal with one of the most sophisticated markets in the world, only then will we benefit.
>
> The reality is we should highlight and raise the profile of the success stories and champion the people and companies who have come to Japan and had a go. It is those organisations that have come here and seen a niche area where they can make a difference, it is those organisations that have created opportunities and have started to do business."

On the value of preparation and building relationships with Japanese counterparts:

> "Preparation is essential when visiting Japanese counterparts; many questions will be asked in an attempt to understand the detail around processes or market information. These questions might sometimes be seen to be time intensive, laboured and bureaucratic but they need to be dealt with. It is simply about the process of being prepared and realistically saves a lot of time later. What is also vital is to stay in contact, follow up properly and build a relationship that goes past the initial visit."

On learning from non-Australian company successes in Japan:

> "A common theme of non-Australian companies that have done well in Japan is their emphasis on authenticity, working hard to develop their brand and the story behind their service or product. For example, NZ company Zespri has released catchy new advertising recently which has gone viral. This has resulted in people at supermarkets scrambling to get Kiwi fruit for their family, resulting in solid sales and market share growth. Scandinavian companies have tailored their marketing and marketing presence by focusing on socially sustainable trends and being forward-thinking: irrespective of whether it is furniture or lifestyle goods, they demonstrate high quality."

On innovation in Japan:

> "56 per cent of the worlds companies that are over 200 years old are in Japan. These companies would not have survived if innovation was not part of their DNA. To me, this demonstrates that these companies are constantly evolving and attempting to bring about change in order to stay relevant. There is an opportunity for Australian companies to be part of this transformation."

Best practice in external affairs: Managing your stakeholders, brand and reputation in Asia

BEST PRACTICE IN EXTERNAL AFFAIRS: MANAGING YOUR STAKEHOLDERS, BRAND AND REPUTATION IN ASIA

By Penny Burtt, Group Chief Executive Officer, Asialink and Mukund Narayanamurti, Chief Executive Officer, Asialink Business

INTRODUCTION

Capabilities in external affairs are vital for both navigating risks and creating value in Asian markets. Too often Australian companies focus on the issues of bribery, corruption and regulatory complexity in Asian markets, the impact these issues could have on their corporate brand and reputation without adequate consideration of the strategy and structure of their external affairs function – the very function essential to manage these issues.

Understanding how the best multinationals organise and execute their external affairs is core to managing stakeholders, brand and reputation in Asian markets. Focusing on and bolstering the external affairs function is the most robust approach to managing issues and crises in Asian markets, and the possible impact on market perceptions and the share price of companies committed to business engagement in the region.

One of the region's leading external affairs experts, Anna Whitlam, says: "The discipline of external affairs has changed so much in the last 10 years – from a tactical crisis response to playing a significant role in mitigating risk and enabling market access. Today's external affairs leader is also the organisation's Chief Sense-Maker! They are experts in synthesising data, news and information in the internal and external environment, using their judgement to feed into group executive, CEO and board to enable sound decision-making."

In an insightful discussion with Anna Whitlam, Alan Butler, the former head of Diageo's centre of excellence for policy and public affairs, said: "Hope that the current volatility passes is simply not a strategy. Organisations dependent on a global view must have a geo component to their business strategy. To ensure a business is prepared for the complexities it will undoubtedly face, it must develop its own version of corporate foreign policy and ensure there is an external radar influencing business decision-making"[48].

Recent research by Weber Shandwick[49] has confirmed that reputation makes a meaningful contribution to business success. Global executives attribute 63 per cent of their company's market value to their reputation. In Australia, this is at 58 per cent, Indonesia 73 per cent, Singapore 53 per cent, China 65 per cent, Hong Kong SAR 47 per cent, Japan 58 per cent, the Republic of Korea 63 per cent, and India 69 per cent. These findings highlight that for Australian companies expanding into Asian markets, carefully managing their reputation with a range of stakeholders will be critical.

This section focuses on the value of establishing the external affairs function as a top priority, priority stakeholders to engage with in the region, how the best companies structure their external affairs function, and understanding the role of the media and its influence on Australian companies doing business in Asia.

ESTABLISHING THE EXTERNAL AFFAIRS FUNCTION AS A PRIORITY

In the most effective multinationals operating in Asia, the external affairs function is not perceived as a cost centre – it is seen as a revenue enabler. Core to the role of the function is promoting the role of the company and its value to the Asian markets where it operates – both in market and in its home base/headquarters, protecting the company through anticipating and managing risks (regulatory and reputational), and finding opportunities to partner in-market (with government, NGOs, industry associations and other key stakeholders) on issues of mutual benefit.

Those global companies that are committed to managing external engagement, including reputation, as a key organisational priority have C-suite executives and board members who are focused on the issue.

A recent global survey by McKinsey & Company on external engagement[50] found that senior executives recognised the need to engage stakeholders and were increasingly focused on their companies' efforts in this area. Nearly 60 per cent of respondents said the topic ranks among their CEOs' top three priorities.

Just over half of the survey respondents said the topic has been a top or top three item on their boards' agendas, up from 31 per cent in 2013. CFOs have also been investing time in stakeholder management: one-third of respondents said external engagement is among the top three priorities on their agendas. The emphasis that CFOs have put on external engagement is consistent with other research indicating the potential for strong external engagement to create business value[51].

Leaders' increasing focus has come amid growing evidence that addressing societal issues and stakeholders' priorities creates long-term value[52]. Some respondents – particularly those at organisations that excel at external engagement – said they view external issues as an opportunity.

SHARED VALUE AND SOCIAL IMPACT

Shared value and social impact projects are an important tool for companies investing and operating at scale in Asia. As part of their wider ESG efforts, many major multinationals use social impact or shared value projects in Asia to:

- Create development impact in the communities where they operate;
- Build reputation;
- Engage key stakeholders in government and the community; and
- Extend their consumer base and drive business.

For example, in the case of banks or financial services companies in emerging Asian markets, many of the US multinationals deliver programs to support inclusive growth. These are normally designed to support government efforts to drive financial inclusion and/or financial literacy, entrepreneurship, and micro and small and medium enterprises. They are delivered in partnership with local NGOs or community groups to create social impact through providing access for the unbanked. These programs have a direct business benefit for the company involved through raising their profile and extending their customer base.

A strong example is the work done by the Mastercard Centre for Inclusive Growth in Asia. Their programs include:

- Supporting Women Entrepreneurs in India [53]; and
- The Strive Program for micro-business in Indonesia (with Mercy Corps Indonesia)[54].

Speaking at the 2020 Australian Governance Summit[55], Michael Froman, former US Trade Representative, an executive with Mastercard and board member of the Walt Disney Company, said companies need to look at how to meet environmental challenges and how to be inclusive while at the same time pursuing economic growth.

"I actually think the challenge that companies face is not between shareholders and stakeholders – it's between short-term and long-term," Froman told the summit.

Froman said Mastercard invests in financial inclusion because it is in the company's interest to have inclusive and healthy economies. "If the economy is thriving, then we will thrive as a company," he said.

WHICH STAKEHOLDERS MATTER THE MOST?

In doing business in Asia, the most important stakeholders include government and regulators, industry and business associations, other businesses, local community and NGOs (in the case of investment) and media. Their priority differs significantly from country to country.

The ability of foreign companies to successfully execute business in most Asian markets depends overwhelmingly on having a well-developed understanding of the destination market's policy and regulatory environment. That means not only trade and investment policies, but sector-specific regulations and national development plans and priorities. Companies who can position themselves to contribute on the latter are more likely to succeed over the long term.

For example, a digital payments company that intends to operate in an Asian market needs to understand, at a granular level, data regulations (including on data storage, classification, security, transfer). It also needs to respond to the host government's digital economy policy aspirations – for example the national digital payments road map or digital financial inclusion targets – to align its impact with national priorities. That means having strong links to government and good access at appropriately senior levels.

Our consultations with senior external affairs executives have highlighted that US and Japanese multinationals were generally more effective at shaping the agendas of governments in the region. Australian companies were generally considered to lag behind but were perhaps on par with Chinese companies, who over the last decade in particular have become increasingly more present across the region.

Local industry and business associations can support foreign companies in three important ways: with access to government; information and insights on regulatory issues and industry developments; and networks. They can also provide a platform for messaging and marketing to increase in-market visibility to suppliers and consumers.

While media is an important means of messaging to key stakeholders, it has significant limitations and narrowcast (not broadcast) options are often better platforms for stakeholder engagement. As in Australia, the trend in many Asian markets has been a decline in consumption of mass media in favour of more specifically curated and targeted sharing of insights. While company announcements on major initiatives or company performance are still often made through mainstream media, more targeted communications to shareholders/investors, stock market analysts, government or key industry or community players are more likely to be effective. In some Asian markets, use of the mainstream media for stakeholder messaging is complicated by levels of government control and questions over independence and credibility.

THE SIZE, COMPOSITION AND FOCUS OF AUSTRALIAN EXTERNAL AFFAIRS FUNCTIONS

In most cases US and European multinationals invest significant resources in building their external affairs teams, with a mix of capabilities including communications and media, policy and regulatory, government affairs, corporate social responsibility/social impact, and stakeholder engagement. The external relations team (or teams if the external relations function is split across several teams) is usually represented in the regional and country leadership teams, with members in the Asia headquarters and on the ground in key markets. The team is usually recruited with a broad mix of capabilities and in-country expertise (including language skills). Many companies recruit ex-government officials with either diplomatic or trade policy experience and country-specific expertise and relationships.

The external relations team usually has dual reporting lines – to headquarters in the US or Europe and then within Asia, both functionally and geographically. That, of course, also varies significantly from company to company.

In addition, many US and European multinationals supplement their external affairs capability with additional, market or function-specific consultancy support. There are many specialist consulting firms delivering support for multinationals in Asia, ranging from public affairs to specialist regulatory advice. US examples include the Albright Stonebridge Group, who describe themselves as "commercial diplomats" offering strategic advisory and The Asia Group, specialising in serving leading companies wanting to "excel in Asia". While there are some limited offerings by Australian consulting firms, few provide the in-market expertise and networks of their US and European counterparts. Australian companies are often reluctant to invest in the cost of additional expert advice.

Most Australian companies operating in Asia have a limited external relations presence in the region, including at the individual country level. Of the larger Australian companies, some have external affairs representation in regional headquarters. However, the size of the external relations presence is often smaller than US or European company teams.

Many Australian companies, however, try to manage the external relations portfolio from Australia on a fly-in/fly-out basis. That detracts from their ability to build in-market relationships and networks, have ready and timely access to information on policy and regulatory developments, and an understanding of and contacts in the media. Few Australian companies deliberately identify Asia capability as a core competence in their external relations teams (or wider leadership teams).

Likewise, few Asian multinationals have well-developed external relations teams. Many rely on networks of senior advisors or external consulting support in target markets to assist with navigating communications and stakeholder engagement opportunities and challenges – rather than in-sourcing the capabilities. The increasingly notable exceptions are large Chinese companies that have encountered significant reputational, regulatory or governance challenges in key markets. Those companies have started developing external relations capabilities, modelling themselves on the US multinationals, albeit with a more limited in-market presence.

MEDIA ENGAGEMENT AND ITS INFLUENCE ON AUSTRALIA – ASIA BUSINESS ENGAGEMENT

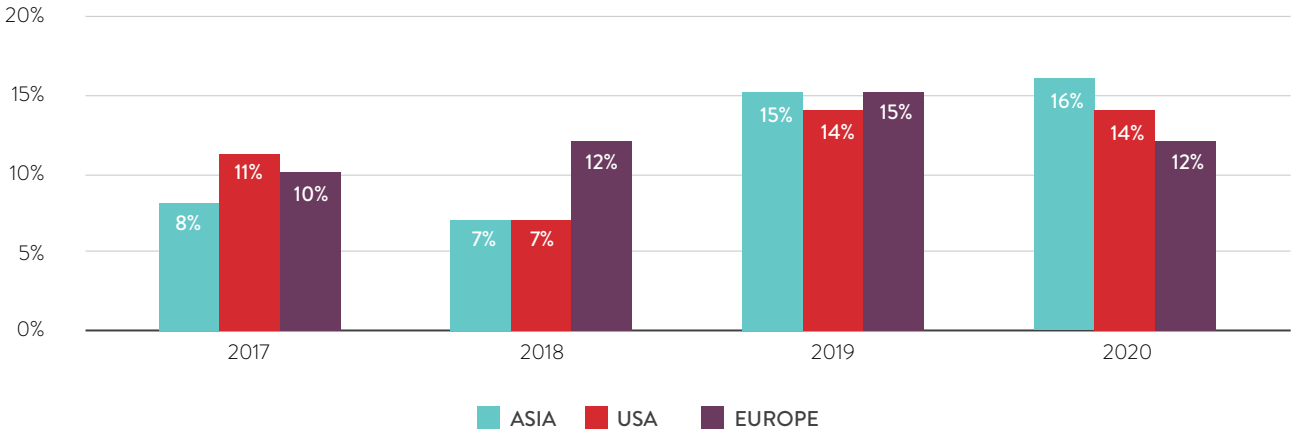
A strongly held view among Australian corporate leaders is the negative sentiment represented in the media on doing business with Asia. *Match Fit*[56] highlighted that this may be due to the negative sentiments of sell-side analysts and the risk aversion expressed by boards and senior executive teams.

Our research highlights that, over the last three years of media reporting on economic and business issues, there is limited evidence to suggest that the media is more or less positive, negative or neutral on Asia than other regions, in particular the US[57]. The election of Donald Trump as the US President has dramatically changed the sentiment towards the US. As figures 1, 2 and 3 highlight, reporting on Asia has generated almost as much positive sentiment as the US in 2017 and 2018, but is below Europe. In 2019 and the first half of 2020, positive media sentiment in respect of Asia is ahead of the US. Reporting on Asia has generated similar levels of negative media sentiment compared to the US over the last few years. In the first half of 2020, media sentiment in relation to the US is more negative than Asia.

Some themes that have dominated media reporting on Asia include:

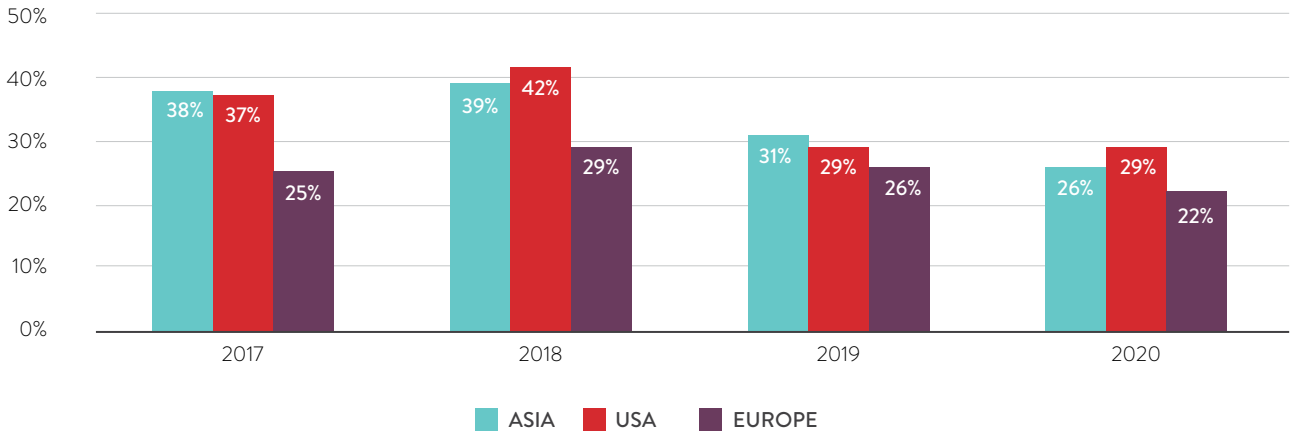
- More recently Asia coverage has been dominated by Australia-China tensions, including over COVID-19 and trade.
- President Trump has remained a fixture within the news regarding Asia since his election in 2017. This is in part due to his hawkish stance towards China, which has only increased in intensity.
- Much of the media's attention in relation to China has been focused on the tit-for-tat between the two leaders (from China and the US) imposing tariffs and the flow on effect to the global economy. This see-sawing of relations between the two countries has often precipitated rises and falls in various stock markets.
- Investor sentiment was improving in 2019 compared to 2018 in light of the commitment towards completing phase one of the US-China trade deal.
- Several events in 2020 precipitated a sharp decline in investor sentiment, none more than the advent of the novel coronavirus and its rapid spread. Increasing tensions in Hong Kong, Australia's push for an independent inquiry and the increasing reservations over the Belt and Road Initiative have all dominated reporting.
- There has been some traction towards a push for increased focus on 'safer' alternative markets such as Vietnam and India.

FIGURE 29. *Positive media sentiment*



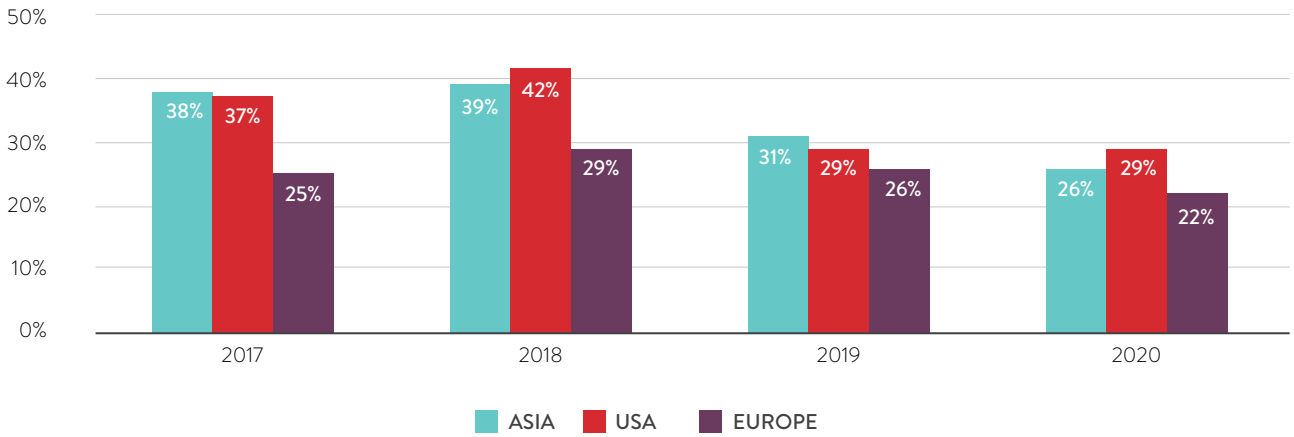
Source: Meltwater: Sentiment analysis

FIGURE 30. *Negative media sentiment*



Source: Meltwater: Sentiment analysis

FIGURE 31. *Neutral media sentiment*



Source: Meltwater: Sentiment analysis

THE ROLE OF THE MEDIA IN ENABLING ASIA ENGAGEMENT

By Peter Cai, Non-resident Fellow at the Lowy Institute

The media plays an important role in creating the folklore and overarching narrative around Asia.

Despite the overwhelming economic and strategic importance of the region, Australian media pays surprisingly insignificant attention to our immediate neighbourhood. For example, none of Australia's newspapers maintain a bureau in Japan or South Korea, our second and third-largest trading partners. Instead, we devote our limited foreign correspondent resources to cover London and Washington, two countries where we can source a whole array of English news sources.

When commercial media covers Indonesia, the most important Southeast Asian country, stories that hog headlines are often about drug dealers and boat people. As a reporter, when I interviewed the Indonesian Ambassador to ASEAN, he wagered that my editor would not run the story for the simple reason that "no one is interested in an Indonesian story" and he was right.

Another example is India. The media coverage of the second most populous country in the world and an emerging tech superpower often revolves around food, Bollywood, slums and Delhi crimes. It is incredulous that many Australian executives have not heard of the Indian Institutes of Technology (IITs), a series of elite institutes that breed some of the most influential tech leaders in the Silicon Valley. There is little coverage in the Australian media of the Indian economy, Indian business or the Indian diaspora community in Australia which is growing in size and influence.

Given the prevailing Asia narrative, it is important that Australian senior executives communicate better with journalists about the importance of Asia. Australian media is facing the twin challenges of ever-shrinking resources and the need to cover better and more deeply our diverse and complex region. Companies should do more than offer 'junkets' to reporters to go to Asia; instead they should support Australian media to develop Asia literacy across the board.

Two good examples are The Judith Neilson Institute and Westpac. The Neilson Institute has helped *The Australian Financial Review* to re-establish its Indonesian bureau after years of neglect, allowing the premier business paper to cover the country's most important Asian neighbour. It is also sponsoring *The Australian* to cover the region's Chinese diaspora communities, a diverse, large and influential group in the region.

Westpac, through its foundation, is helping young scholars to better understand Asia through a major scholarship program. Other corporates could follow the Westpac formula by sponsoring reporters to better understand Asia through fellowship programs that allow them to live, study and work in the region, with a focus on covering business and economics.

Companies are increasingly devoting more resources to issues such as environmental awareness, gender equality, ethnic diversity and indigenous empowerment as part of their corporate social responsibility program. Helping the country's media to develop strong Asia literacy should be added to the list of worthy causes.

Companies do bring interesting Asian leaders to Australia and often for the benefit of their clients and stakeholders. We can bring them out from behind closed doors and share opportunities with the public more often. I remember how my interest in India was sparked by attending a fascinating talk by Nandan Nilekani, the legendary IT guru who started Infosys.

AMP and the Lowy Institute's partnership is a good example. This program enables the Institute to bring out Chinese business and opinion leaders to visit Australia through a public program of visits and talks. One example is Hu Shuli, an internationally respected business editor from Beijing. Corporate Australia has a special responsibility to help our shrinking media with fewer and fewer resources to develop Asia literacy.

There is little doubt about the economic and business importance of Asia for Australian businesses.

RECOMMENDATIONS

There are five ways Australian companies can more effectively organise their external affairs function to deliver greater value in engaging with Asia, including through media engagement.

1. Asia-capable talent and a distributed organisational structure

Recruiting Asia-capable talent should be an absolute priority. This includes Australian expatriates with deep Asia experience, Asian-Australians with continuing business links to the region, and Australian executives more broadly who reflect the essential capabilities to succeed in Asian markets[58]. We recommend against treating Asian market opportunities as merely a reward for talent to develop in-market experience. Recruiting in-market talent and building teams on the ground in key markets is vital.

We also recommend that there is more of an onus placed on strengthening in-market teams, where leaders of these teams sit on the regional leadership team and partner with regional executives (for example the regional CEO) on executing the organisation's Asia strategy. We recommend a lesser focus on a fly-in/fly-out strategy. As previously highlighted, a fly-in/fly-out strategy detracts from the ability to build in-market relationships and networks, have ready and timely access to information on policy and regulatory developments, and an understanding of and contacts in the media.

> *"In some markets where it is difficult to secure experienced external affairs talent, many multinationals use local agencies to access local governments and media, however if your organisation has a long-term plan to invest in a particular market, look to invest in the community by developing local talent and capability. If you make a choice to start investing in key markets today, in time, your in-country external affairs leaders will be superstars."*
>
> Anna Whitlam, Founder and Managing Director, Anna Whitlam People (stakeholder consultations)

2. Involve the C-suite with active media engagement in Asian markets

Our consultations with leading journalists based in Asia highlighted that the companies that engage the best with the media create a culture of their senior leaders working in close partnership with their public relations and communications teams. These senior leaders engage with the media confidently when they visit an Asian country. They share the story of their company, their purpose, and the value they seek to deliver to the host country's development, consumers and broader communities. They also seek to share updates over time, enabling the media to build a continuous narrative that converts to a coherent one for both the local audience and home country audience. This sophisticated approach also recognises that while narrowcast options are best to influence particular stakeholders in a targeted way, with increasing nationalism in many markets governments and regulators also pay regard to the reaction of the broader community to foreign companies.

"The most savvy invest in building relationships with the media. Senior leaders who meet with the media when they visit are most effective. They chat more confidently, more regularly and share interesting views. They complement the efforts of their PR and Communications teams."

Michael Smith, China correspondent, The Australian Financial Review (stakeholder consultations)

"To shift what is happening it is important for Australian companies to share the success of their strategies in Indonesia. Indonesian media are also keen readers of what the Australian media report about Indonesia. What you end up doing is reflecting a lens back to the Indonesian readers which is important. There is this idea with some of the more traditional Australian companies that they can go there and not present to the local population what's going on."

Emma Connors, South-East Asia correspondent, The Australian Financial Review (stakeholder consultations)

3. Transition from risk aversion to a growth mindset and from a focus on failures to success

The perception that the media presents a negative sentiment can be addressed practically through at least three strategies. First, a recognition that this is not unique to Asian markets. As the media sentiment analysis highlights, in recent years reporting on Asia has included at times more positive sentiment than reporting on the US. Second, Asia-capable boards and senior executives should engage with the media to share their successes in Asian markets. Risk aversion is pervasive in the Australian environment. Measured presentations on the long-term risk-adjusted returns in Asian markets help position the company as a growth company. Third, industry bodies, chambers and professional services firms have an important role to play in sharing case studies of companies that have succeeded in Asian markets.

"The US media is generally kinder to their companies in China, except for maybe the last four months. The American Chamber in China plays a very important role. The US media generally reports on successes well."

"US and European companies have a history of going out and doing well. We have less exposure to our companies overseas as they do fewer offshore deals."

Michael Smith, China correspondent, The Australian Financial Review (stakeholder consultations)

4. Define the external affairs function as a revenue enabler and not a cost centre

Given the research which indicates that the external affairs function does not just navigate risks but creates significant organisational value, it is essential that it is positioned as a revenue enabler rather than as a cost centre. We recommend alignment with strategy, product and business development teams in respect of the short-term and long-term incentives on offer on the achievement of business objectives and targets. While most C-suite executives are rewarded on measures ranging from earnings per share to total shareholder return, we recommend that similar measures are applied for the external affairs team. There should be greater weighting towards long-term measures, recognising the long-term intangible impact of reputation on a company's market value.

We also recommend that the focus of the external affairs team should be on broader stakeholder engagement, going beyond media and communications and marketing. Framing the role of the function in this broader way enables a stronger connection to the organisation's strategy and performance.

Making external engagement a CEO priority and creating a culture of the external affairs team partnering with the C-suite and board on external engagement creates a better coordinated, aligned and more robust organisation.

5. Support an organisational design that facilitates seamless integration and agility

Our consultations highlighted the seamless, integrated nature of the best-performing external affairs teams. The formula for combining local expertise with parent company context is critical to ensure long-term success.

"Companies that do it well have regional CEOs in Australia, Singapore and other countries, who see government or external affairs as a business opportunity. They have a global public policy and government/external affairs function that sits in London; they are integrated in such a way it is like they are all sitting in the same room, even though they are across multiple countries, they share the same strategy. They have local implementation, they hire locally and still bring in expats but in-country they value the local expertise and cultural understanding as they know how important it is going to be. They also want to reward their people that way. They want to see how they can reward their external affairs for directly enabling business opportunity and growth, it is extraordinary.

Certain mining companies that do this well are very focused, move resources around, and deliver via an integrated global strategy. They understand what they will need in key markets and they invest to enable outcomes."

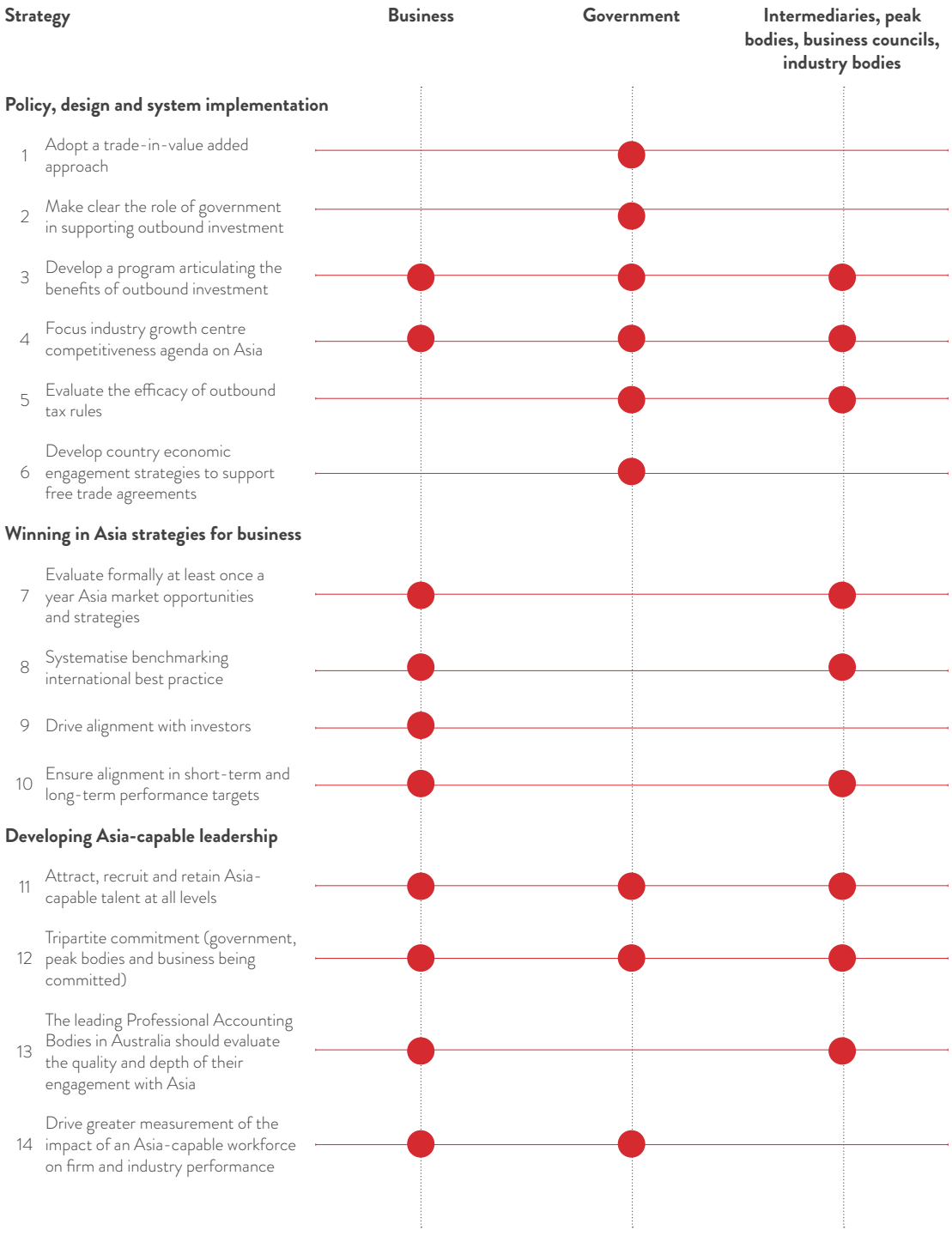
Anna Whitlam, Founder and Managing Director, Anna Whitlam People (stakeholder consultations)

A strategic approach to winning in Asia

A STRATEGIC APPROACH TO WINNING IN ASIA

The strategies in this section provide an overall approach to winning in Asia. These strategies should be read in addition to the very specific strategies in the previous two sections (applying to board and senior executive capabilities and external affairs).

FIGURE 32. *A strategic approach to winning in Asia*



1. Adopt a trade-in-value added approach

The section on **'Does offshore expansion lead to superior returns?'** highlights that there is still significant untapped potential in Asian markets for Australia's services sector. As efforts are made by policymakers to facilitate more services sector engagement with Asia, consideration should also be provided to how trade data is captured and reported.

Trade data currently reflects the performance of the Australian export economy in direct export terms. Services exports do not currently reflect the value of services embodied in the production of commodities and products. It also does not include foreign affiliate sales of Australian companies. As Australian companies transition towards the delivery of a range of services to Asian economies, it will become increasingly likely that they will deliver services through their subsidiaries in offshore markets. The need to be close to the end consumer in the services sector will drive the offshore presence of Australian businesses delivering the services. In the absence of a trade-in-value added approach these offshore foreign affiliate sales will not be captured in Australian trade data.

2. Make clear the role of government in supporting outbound investment

As reflected in the section on **'How the best 'win in Asia': Business models from companies succeeding in Asian markets**" the most successful Australian companies in Asia (across sectors) invest significant capital to establish an on-the-ground presence in host markets. Our consultations revealed a lack of understanding by business of the role of government in supporting outbound investment. Historically, the Australian Trade and Investment Commission (Austrade) has focused on Australian exports, international education, tourism and inbound investment.

More recently, the explicit reference to growing outbound investment from Australia to India in the India Economic Strategy to 2035 has raised the importance of outbound investment being actively facilitated by Austrade and the Department of Foreign Affair and Trade (DFAT). Recent bespoke trade missions to India for Australian superfunds, facilitated by DFAT and Austrade, signal the Australian Government's support of outbound investment. Both DFAT and Austrade have excellent networks and market knowledge which together with the 'badge of government' would be invaluable to Australian companies seeking to invest in Asian markets. Their roles in supporting outbound investment should be made clearer to business.

3. Develop a program articulating the benefits of outbound investment

Our consultations revealed the highly politicised nature of outbound investments. This should be systematically addressed to facilitate the growth in offshore revenues and returns of Australian companies. While most countries actively seek to attract foreign investment into their markets, there is less open support for the idea of outbound investment. There is an often-stated view of governments that the capital of domestic companies should be invested in the domestic market rather than in offshore markets. This is seen as enabling home country jobs and economic development. The deployment of capital in the home market rather than offshore is also seen as beneficial in delivering more stable returns in an environment in which there is greater institutional and regulatory certainty for local capital providers. Governments also often prefer onshore capital deployment to generate new assets, capabilities and taxes. However, these arguments can prevent high-quality opportunities in offshore markets being pursued: in particular those opportunities that offer scale, a superior return on capital, and global talent to be secured.

As the World Bank highlights, "there is growing evidence that outward foreign direct investment (OFDI) can increase a country's investment competitiveness, crucial for long-term, sustainable growth"[59]. The World Bank sees OFDI as "a natural extension of export promotion"[60].

We recommend a coordinated approach to advocating to the community the benefits of outbound investments to selected Asian markets that are critical economic partners of Australia. This is also critical in ensuring our relationships evolve to genuine engagement which comes from committed capital and 'boots on the ground'. Our Asian partners – in particular in South-East Asia, India and China – are actively seeking and expect foreign capital to flow to their economies from their relationship with Australia. Australia's superfunds are often of great interest to our partners seeking long-term investments, in particular for infrastructure development. Educating the community of the benefits of investing Australian capital in Asian markets would make it less unpopular in the local context.

4. Focus industry growth centre competitiveness agenda on Asia

Industry competitiveness is highly dependent on workforce skills. **'Match Fit 2.0: Creating Asia-capable leaders'** highlights the acute shortage of boards and senior executive teams that are Asia-capable. The six industry growth centres are central to Australia's global competitiveness. As part of boosting sector productivity, we believe that following the lead of MTPConnect, each growth centre should develop and implement a comprehensive program of work related to Asian markets. MTPConnect has been exceptionally active in leading Australian medtech and pharma companies to pursue market opportunities in South Korea, India, Singapore, China, Hong Kong and Indonesia. Food Innovation Australia Limited (FIAL) has also been central to Australian food exporters being internationally competitive.

We recommend that our industry growth centres place the key markets of China, Hong Kong, India, Indonesia, Singapore, Japan and South Korea as a focus in their program of work. In addition, we recommend that following the lead of MTPConnect, they develop a qualified database of Asia-capable board members and senior executives in their respective sectors.

5. Evaluate the efficacy of outbound tax rules

Our consultations for the section on **'How the best 'win in Asia': Business models from companies succeeding in Asian markets'** revealed that tax considerations were not immaterial when considering doing business in the region. In particular, the inability to pass on offsets to Australian shareholders for foreign tax paid is an impediment to securing support from investors. Australia's controlled foreign company, transfer pricing, capital gains, interest, royalty and dividend repatriation rules should be considered in terms of their ability to support increased outbound investment. There should also be increased education of Australian businesses by the Big Four firms, the Tax Institute and peak bodies such as CA ANZ and CPA Australia of the tax risks in the operating environments in Asian markets.

6. Develop country economic engagement strategies to support free trade agreements

Our consultations for the section on **'How the best 'win in Asia': Business models from companies succeeding in Asian markets'** revealed that the India Economic Strategy to 2035 had led to a significantly greater awareness of opportunities with an Asian market (India) compared to countries with which Australia had a free trade agreement only (e.g. Republic of Korea). We recommend that complementing the Australian Government's highly successful track record of concluding free trade agreements (FTAs), should be publicly available country economic strategies for key economic partners. The India Economic Strategy to 2035 was developed while FTA negotiations were still being undertaken with India. The strategy with India offers a clear blueprint of the major sectors and states with which Australia should pursue opportunities. It offers a fundamentally different value proposition to an FTA with India, which (should one be concluded) reduces barriers to trade and investment between the two countries. With the strategy in place the FTA is more likely to be utilised if concluded.

We recommend a comprehensive strategy for Indonesia – similar to the India Economic Strategy to 2035. This will complement IA-CEPA and enable Australian businesses to more deeply understand the opportunities with this critical market. We also recommend that similar to the India Economic Strategy to 2035, the strategy with Indonesia should have an ambitious outbound investment target.

7. Evaluate formally at least once a year Asia market opportunities

Our consultations revealed the extensive use of outdated anecdotes and sentiments on Asian markets in the Australian corporate sector. These are primarily centred on the challenges of doing business in the region, the perceived risks, and the inability to generate high returns. We recommend that ASX 200 companies and large private companies annually assess opportunities with Asian markets.

A senior leadership team committed to an Asia strategy is essential for organisational success. Our consultations have highlighted the challenges middle management often faces in securing senior leadership support of projects pursuing Asian growth. It is also essential that by reviewing opportunities regularly senior leaders rely on up-to-date research in informing their decisions to pursue or not to pursue opportunities.

The dynamic and high context nature of Asian markets requires annual assessments. It will ensure that the impact of the use of outdated anecdotes on doing business with Asian markets is limited. We recommend **Lendlease** as best practice in macro and micro analysis of market opportunities in Asian markets.

8. Systematise benchmarking international best practice

Our consultations highlighted that offshore expansion will become more likely once Australian companies start to embrace international best practice in organisational design and strategy. This includes best practice in technology adoption, management practices, governance, planning for the future of work etc. As Asian companies continue to grow and become globally dominant enterprises, it will become increasingly likely that Australian companies will partner with Asian companies in Australia, the host country or third markets. We recommend that on an annual basis ASX 200 companies refresh their library of case studies of best practice in Asian markets. This should cover innovation and new product development, sales, marketing and distribution strategies, capital market developments (equity and debt), workforce development patterns, and management practices. The consistent growth in the number of Asian companies on Forbes' annual listing of the world's most innovative companies, provides evidence of the ability of these companies to generate a superior 'innovation premium' for their shareholders. Studying the underlying methodology for the determination of 'innovation premium' (using Credit Suisse's proprietary HOLT methodology) is useful in developing an approach to generating superior shareholder value.

9. Drive alignment with investors

Our consultations as reflected in the section on **'Engaging with investors'** have highlighted three aspects to best practice in investor relations. First, the need to articulate a clear, consistent and long-term strategy. Second, to not let investors determine your strategy but to use your strategy to attract the types of investors aligned to your strategy. Third, taking investors on an informed journey is crucial. For instance, annual tours of global operations is seen as highly effective in helping investors understand market opportunities.

10. Ensure alignment in short-term and long-term performance targets

Our consultations highlighted the need for there to be a strong mix of short-term and long-term incentives for senior management that was aligned with the objectives of the organisation. There was a recognition that short-term incentives were essential to meet quarterly, bi-annual and annual metrics. However, most of the companies we evaluated had long-term incentives comprising at least 50 per cent of the incentive structure. This balance ensured that these companies were better positioned to deliver long-term results from Asian markets.

11. Attract, recruit and retain Asia-capable talent

A consistent theme through all sections in this report is the need for Asia capabilities to identify, evaluate and execute opportunities effectively with Asian markets. Asia-capable talent is central to this proposition. We recommend a three-pronged strategy to identifying Asia-capable talent.

- **Work with the various business councils to identify networks of Asia-capable individuals:** The Asian business councils in Australia are a highly underutilised network of platforms. The Australia China Business Council, the Australia India Business Council, the Australia Indonesia Business Council, the Australia Korea Business Council and the Australia Japan Business Cooperation Committee all offer exceptional access to networks of professionals who offer the insights, capabilities and connections Australian businesses are seeking to expand into Asia. There is significant under-representation of the ASX 200 in the membership of these councils. This is often a first and essential step to committing to learning about Asian market opportunities, the critical role of government (in Australia and in the region), and best practice in winning in Asia. This approach complements in-house expertise and the use of consultants to advise on bespoke strategies.
- **Identify and elevate Asian-Australian talent:** More work needs to be done to identify and elevate Asian-Australian talent, including through initiatives like the Asian-Australian Leadership Summit (AALS) and professional groups such as the Asian-Australian Lawyers Association.

Australia's large and growing Asian-Australian community (over 12 per cent of the population) offers a significant pool of Asia capability. Companies should work actively to engage those individuals through initiatives like the AALS and professional associations. The AALS provides businesses with a unique opportunity to engage with exceptionally qualified Asian Australians, understand their perspectives, and create a market-leading strategy for diversity that includes Asian Australians. Representation at the inaugural AALS in 2019 revealed strong participation from universities, government, professional services firms, and community groups. Significant potential remains for greater levels of engagement by ASX 200 companies and large and medium sized private enterprises with the AALS in the future.

- **Collaborate with organisations like Advance, the Australian Chambers of Commerce in the region and executive search firms to leverage Australian expatriate talent:** Advance connects 'global Australians with one another and with Australia'. With the support of a powerful board, global ambassadors, corporate partners, sponsors, and patrons, Advance recognises and celebrates the achievements of global Australians[61]. Increasingly their focus is on Australian expatriates in Asia. As reflected in the section on **'Match Fit 2.0: Creating Asia-capable leaders'**, the profile of Melanie Brock (Global Ambassador, Advance) is a powerful example of the exceptional talent Australian expatriates based in Asia can offer. The Australian Chambers of Commerce across several Asian markets also offer connections at scale with Asia-capable Australian expatriates.

  Our previous work in 'Match Fit: Shaping Asia-capable leaders' highlighted the critical role of executive search firms in informing board nomination committees of the value of this untapped community. This is still an early stage work-in-progress with much room for improvement.

12. Tripartite commitment (government, peak bodies and business being committed)

Our consultations revealed a strong appetite for coordinated action to shift the thinking of corporate Australia towards improved engagement with Asia. A transformation of the capabilities of board members will ultimately depend on significant commitment from a range of stakeholders including corporate boards, government and peak bodies. Cooperation and cross-sector collaboration supported by the Australian Government will be critical in ensuring that the development of Asia capabilities becomes a strategic focus for boards.

A multi-disciplinary approach could include initiatives aimed at monitoring progress of Asia capability in leadership, the creation of capability and development opportunities for business leaders, and a cross-sector campaign aimed at highlighting the business case and growth opportunities for Australian businesses. Building on these recommendations, the AICD and Asialink Business will work together to identify further opportunities to increase Asia capability on boards.

13. The leading Professional Accounting Bodies in Australia should evaluate the quality and depth of their engagement with Asia

The leading accounting bodies in Australia, CA ANZ, CPA Australia, IPA, and the ACCA are the conduits for future Chief Financial Officers (CFOs). CFOs play a critical role with capital allocation strategies which becomes even more complex when allocating capital in Asian markets and driving superior returns. These accounting bodies have deep connections and engagement with Asian markets. We recommend that these accounting bodies continue to evaluate all facets of their engagement with Asian markets from the quality of Asia related content in their programs to member engagement.

14. Drive greater measurement of the impact of an Asia-capable workforce on firm and industry performance

We recommend that organisations take a capability lens to engaging Asian markets. A capability lens suggests that key individual and organisational capabilities will be essential for success in Asian markets. We recommend that organisations determine a baseline score of the level of Asia capabilities in their workforce. Specific interventions across training, coaching and information should be made available to executives to improve their Asia capabilities from the baseline. Annual measurement of firm level Asia capabilities in parallel with performance in Asian markets will enable a robust evaluation of the impact of capabilities on performance.

Notes

NOTES

The analysis undertaken by BCG on **'Does offshore expansion lead to superior returns?'** uses a cut-off date of 30 September 2019, unless noted otherwise. Company financials from public announcements use financial years, unless noted otherwise.

All amounts in this report are in AUD unless otherwise specified.

1 IMF (2020), World Economic Outlook Update.

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31 Greater than 10 per cent of revenues in 2019 from foreign sources

32 Less than 10 per cent of revenues in 2019 from foreign sources

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- Mateev and Andonov, 2016: Do cross-border and domestic bidding firms perform differently? New evidence from continental Europe and the UK
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34 Total returns runs from 30/09/2009 to 30/09/2019. Comparable benchmarks include US (S&P 500 Consumer Staples), Europe (S&P EUROPE 350 – Consumer Staples) and Asia (MSCI AC Asia Pacific – Consumer Staples).

35 Due to insufficient sample sizes, five industries were omitted from study (banks, communications, healthcare, insurance and utilities).

36 The measures of international diversification tested were average percentage share of foreign revenues over a period and change in percentage share of foreign revenues over a period. Simple correlation analysis and multiple linear regression analysis, controlling for industry and domestic revenue growth, were used to test for a relationship between each of the above measures of international diversification and TSR over five-year (2014-2019) and 10-year (2009-2019) periods. Correlations in the simple regressions were below 0.1 in all cases, and P-values in the Multiple Linear Regressions were always greater than 0.1, suggesting statistical insignificance of the variables at a 10 per cent level.

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57 Our research was undertaken in collaboration with Meltwater. Meltwater: Sentiment is done by Natural Language Processing. It analyses the keywords either side of chosen keywords and gives it an overall sentiment rating by the volume of positive, negative and neutral keywords analysed. It is around 70-80% accurate which is the highest accuracy for machine-based sentiment on the market. Based on a prescribed set of words, over the period of 1 January 2017 to 31 May 2020 the system analysed a total of 3,189 articles on Asia, 2,853 on the US and 1,061 on Europe respectively.

58 As reflected in the section on senior leadership capabilities, the essential Asia related individual capabilities include: (1) a sophisticated understanding of markets (2) lived experience typically greater than 2 years in at least one market (3) cross cultural competency (4) language proficiency in one or more Asian languages (5) deep and trusted relationships (6) an understanding of how government works at all levels. These capabilities should be considered with a country lens rather than a generic Asia lens.

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GLOSSARY

CAGR – Compound Annual Growth Rate

EMEA – Europe, Middle East and Africa

ESG – Environmental, Social and Governance

SBI – State Bank of India

SOEs – State-Owned Enterprises

TSR – Total Shareholder Return

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